

This cover page contains certain information for quick reference only. It is not a summary of the issue. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

OFFICIAL STATEMENT

STATE OF TENNESSEE

\$11,885,000 General Obligation Bonds, 2004 Refunding Series A (Federally Taxable) \$42,950,000 General Obligation Bonds, 2004 Refunding Series B (Federally Taxable)(Variable Rate Bonds)

Dated: June 1, 2004

Due: March 1 as shown on inside front cover

<i>Series A Bonds</i>	<p>Interest payable semi-annually March 1 and September 1, commencing September 1, 2004.</p> <p>Interest rates and reoffering prices/yields as shown on the inside front cover.</p> <p>Fully registered bonds in denominations of \$5,000 or any integral multiple thereof.</p> <p>Not subject to redemption prior to maturity.</p> <p>See “The Bonds – Series A Bonds” herein.</p>
<i>Series B Bonds</i>	<p>Initially issued to bear interest at Extended Rates, subject to conversion to bear interest at other Variable Rates (Daily, Weekly, Monthly, Quarterly or Semiannual) and to the Fixed Rate, upon notice and subject to mandatory tender for purchase as described herein. Interest rates and reoffering prices as shown on the inside front cover. This Official Statement has been prepared solely for use in connection with (i) the offering of the Series A Bonds and (ii) the offering of the Series B Bonds, and generally describes the terms of the Series B Bonds only while bearing interest at Extended Rates and is not intended to describe the terms of the Series B Bonds after conversion to bear interest at any other Variable Rate or a Fixed Rate as described herein.</p> <p>Interest payable on each Interest Payment Date commencing September 1, 2004.</p> <p>Fully registered bonds in denominations of \$5,000 or any integral multiple thereof.</p> <p>Subject to optional and mandatory sinking fund redemption, and as described herein.</p> <p>Subject to mandatory and optional tender for purchase as described herein.</p> <p>See “The Bonds – Series B Bonds” herein.</p>
<i>Security</i>	Direct general obligations; pledge of full faith and credit. See “Security for the Bonds” herein.
<i>Book-Entry Only</i>	The Depository Trust Company. See Appendix D.
<i>Tax Exemption</i>	Interest is includable in gross income for Federal income tax purposes. In the opinion of Bond Counsel, the Bonds, and the interest thereon, are free from Tennessee taxes, subject to certain exceptions. See “Tax Matters” herein.

The Bonds are offered when, as and if issued and received by the Underwriters, subject to certain conditions, including the approval of legality by Hawkins Delafield & Wood LLP, Bond Counsel to the State. Certain legal matters in connection with the Bonds are subject to the approval of the Attorney General and Reporter of the State of Tennessee, as counsel to the State, and Bass, Berry & Sims, PLC, counsel to the Underwriters. The Bonds are expected to be delivered in New York, New York, through the facilities of The Depository Trust Company on or about July 7, 2004.

UBS FINANCIAL SERVICES INC.

CITIGROUP

MERRILL LYNCH

MORGAN KEEGAN & COMPANY, INC.

June 23, 2004

\$11,885,000 GENERAL OBLIGATION BONDS, 2004 REFUNDING SERIES A (FEDERALLY TAXABLE)

<u>Due March 1</u>	<u>Amount</u>	<u>Interest Rate</u>	<u>Price</u>	<u>Cusip Number*</u>
2005	\$1,925,000	2.09%	100.00%	880541DC8
2006	1,365,000	2.97	100.00	880541DD6
2007	1,260,000	3.60	100.00	880541DE4
2008	1,535,000	4.06	100.00	880541DF1
2009	1,355,000	4.46	100.00	880541DG9
2010	1,415,000	4.69	100.00	880541DH7
2011	1,480,000	4.91	100.00	880541DJ3
2012	1,550,000	5.10	100.00	880541DK0

**\$42,950,000 GENERAL OBLIGATION BONDS, 2004 REFUNDING SERIES B
(FEDERALLY TAXABLE) (VARIABLE RATE BONDS)**

<u>Due March 1</u>	<u>Amount</u>	<u>Initial Extended Rate Period (Both Dates Inclusive)**</u>	<u>Extended Rate for Initial Extended Rate Period**</u>	<u>Price</u>	<u>Cusip Number*</u>
2029	\$42,950,000	6/01/2004 – 2/28/2010	4.82%	100.00%	880541DL8

*These CUSIP numbers have been assigned by Standard & Poor's CUSIP Service Bureau, a Division of The McGraw Hill Companies, Inc., and are included solely for the convenience of the Bondholders. Neither the State of Tennessee nor the Underwriters are responsible for the selection or use of these CUSIP numbers, nor is any representation made as to their correctness on the Bonds or as indicated herein.

**After the initial Extended Rate Period, the Series B Bonds will bear interest at Extended Rates for Extended Rate Periods unless converted to bear interest at another Variable Rate or a Fixed Rate as described herein.

THE FUNDING BOARD OF THE STATE OF TENNESSEE

Phil Bredesen, Governor, *Chairman*
John G. Morgan, Comptroller of the Treasury, *Secretary*
Riley C. Darnell, Secretary of State
Dale Sims, State Treasurer
Dave Goetz, Commissioner of Finance and Administration

STAFF

Mary-Margaret Collier, Director of Bond Finance, *Assistant Secretary*
Pat Haas, Bond Finance Manager

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ISSUER'S COUNSEL

Attorney General and Reporter of the State of Tennessee, Nashville, Tennessee

This Official Statement does not constitute an offering of any security other than the Bonds offered hereby. No dealer, broker or other person has been authorized to give any information or to make any representation other than as contained in this Official Statement, and if given or made, such other information or representation must not be relied upon as having been authorized by the State. This Official Statement does not constitute an offer to sell or a solicitation of an offer to buy, nor shall there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful to make such offer, solicitation or sale.

Certain information set forth herein has been provided by the State. Certain other information set forth herein has been obtained by the State from sources believed to be reliable, but it is not guaranteed as to accuracy or completeness. The information and expressions of opinion herein are subject to change without notice and neither the delivery of this Official Statement, nor any sale made hereunder implies that the information contained herein is correct as of any time subsequent to the date hereof. Any statements in this Official Statement involving estimates, assumptions, and matter of opinion, whether or not expressly so stated, are intended as such and not as representations of fact.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their respective responsibilities to investors under the federal securities laws as applied to the facts and circumstances in this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

NO REGISTRATION STATEMENT RELATING TO THE BONDS HAS BEEN FILED WITH THE SECURITIES AND EXCHANGE COMMISSION ("SEC") OR ANY STATE SECURITIES AGENCY. THE BONDS HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SEC OR ANY STATE SECURITIES AGENCY. NOR HAS THE SEC OR ANY STATE SECURITIES AGENCY PASSED UPON THE ACCURACY OR ADEQUACY OF THIS OFFICIAL STATEMENT. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

In making an investment decision, investors must rely on their own examination of the State and the terms of the offering, including the merits and risks involved.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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STATE OF TENNESSEE

\$11,885,000 GENERAL OBLIGATION BONDS, 2004 REFUNDING SERIES A (FEDERALLY TAXABLE) \$42,950,000 GENERAL OBLIGATION BONDS, 2004 REFUNDING SERIES B (FEDERALLY TAXABLE) (VARIABLE RATE BONDS)

INTRODUCTION

This Official Statement, which includes the cover page and the inside cover page hereof, and the Appendices hereto, including the financial information incorporated by reference in Appendix A, is provided for the purpose of presenting information relating to the State of Tennessee (the "State") in connection with the issuance of the State's \$11,885,000 General Obligation Bonds, 2004 Refunding Series A (Federally Taxable) (the "Series A Bonds") and the \$42,950,000 General Obligation Bonds, 2004 Refunding Series B (Federally Taxable) (Variable Rate Bonds) (the "Series B Bonds") (the Series A Bonds and Series B Bonds are referred to collectively as the Bonds").

This Official Statement has been prepared solely for use in connection with (i) the offering of the Series A Bonds and (ii) the offering of the Series B Bonds, and generally describes the terms of the Series B Bonds only while bearing interest at Extended Rates and is not intended to describe the terms of the Series B Bonds after conversion to bear interest at any other Variable Rate or a Fixed Rate as described herein.

The Bonds will be issued pursuant to the authority of and in full compliance with the provisions, restrictions and limitations of the Constitution and laws of the State, including Title 9, Chapter 9, Tennessee Code Annotated, and various bond authorizations enacted by the General Assembly of the State, and pursuant to a resolution adopted by the Funding Board of the State on May 27, 2004. The Bonds are being issued to refund certain of the State's outstanding general obligation bonds (the "Refunded Bonds") and to pay certain costs of issuance. (See "Proposed Plan of Refunding and Application of Bond Proceeds".)

The Bonds are direct general obligations of the State for the payment of which as to both principal and interest the full faith and credit of the State are pledged. As additional security for the Bonds and the interest thereon, there is also pledged the annual proceeds of certain specific taxes, revenues and fees required to be paid to the State. The Bonds, together with interest thereon, are entitled to the benefit of these taxes, fees and revenues and to share therein pro rata with any other obligations of the State that might be entitled to share therein as provided by Title 9, Chapter 9, Tennessee Code Annotated. (See "Security for the Bonds".)

The capitalization of any word not conventionally capitalized or otherwise defined herein indicates that such word is defined in a particular resolution, agreement or other document and, as used herein, has the meaning given it in such resolution, agreement or other document. The definitions of certain of such terms are summarized in Appendix F to this Official Statement.

THE BONDS

Series A Bonds

Description

The Series A Bonds will be dated June 1, 2004, will mature on March 1 of each of the years and in the principal amounts as shown on the inside cover page, and will bear interest payable semi-annually on March 1 and September 1 commencing September 1, 2004, at the rates per annum as shown on the inside cover page to the registered owners as of the 15th day of the preceding calendar month. Interest shall be computed on the basis of a 30-day month and a 360-day year.

The Series A Bonds will be issuable as fully registered bonds in principal amounts of \$5,000 or integral multiples thereof.

The Series A Bonds are not subject to redemption prior to maturity

Series B Bonds

Summary

This Official Statement has been prepared solely for use in connection with (i) the offering of the Series A Bonds and (ii) the offering of the Series B Bonds, and generally describes the terms of the Series B Bonds only while bearing interest at Extended Rates and is not intended to describe the terms of the Series B Bonds after conversion to bear interest at any other Variable Rate or a Fixed Rate as described herein.

The following chart summarizes certain terms and provisions applicable to Series B Bonds while they bear interest at Extended Rates. These provisions are described in more detail below and in Appendix F hereto.

INTEREST RATE PERIOD	INTEREST PAYMENT DATE AND RECORD DATE	RATE DETERMINATION DATE	DATE ON WHICH RATE BECOMES EFFECTIVE	NOTICE OF RATE	NOTICE PERIOD FOR OPTIONAL TENDER	CONVERSION DATE (when converting from the Stated Rate Period)	CONVERSION DATE NOTICE TO BONDHOLDERS	PAYMENT FOR BONDS TENDERED
Extended Rate Period	Interest: September 1, 2004, and on the first Business Day of each 6th calendar month thereafter. <u>Record:</u> 15th day (whether or not a Business Day) of calendar month immediately preceding Interest Payment Date.	(A) Preliminary Extended Rate determined by 4:00 p.m. on the last Business Day which is at least 30 days immediately preceding the effective date and (B) actual Extended Rate determined not later than 4:00 p.m. on the Business Day immediately preceding the effective date.	Initially, June 1, 2004, and subsequently on the first Business Day of the calendar month following the last day of the prior Rate Period, and extending for 1 year or integral multiples of 6 months in excess of 1 year set by the State.	Written notice from Paying Agent and Registrar to registered owner not later than 5:00 p.m. on the 3rd Business Day following date of determination.	Written notice to Tender Agent not later than 5:00 p.m. on a Business Day not less than 15 days before commencement date of new Extended Rate.	Interest Payment Date on which new Extended Rate Period would otherwise have commenced.	Not less than 30 days before Conversion Date.	Before 4:00 p.m. on Purchase Date in immediately available funds.

Description

The Series B Bonds will be dated June 1, 2004, and will mature on March 1, 2029. The Series B Bonds will bear interest for the Initial Extended Rate Period, which extends to February 28, 2010, at the rate of 4.82% per annum, as shown on the inside cover page of this Official Statement, and thereafter at Extended Rates and for Extended Rate Periods determined as described in Appendix F to this Official Statement unless converted to bear interest at another Variable Rate (Daily, Weekly, Monthly, Quarterly, Semiannual) or at a Fixed Rate, upon notice as described herein. Upon each such conversion, the Series B Bonds will be subject to mandatory tender for purchase, as described herein. The Series B Bonds are subject to optional tender for purchase in conjunction with establishing new Extended Rate Periods, as described herein.

Interest on the Series B Bonds will be payable on each Interest Payment Date, commencing September 1, 2004, to the registered owner as of the applicable Record Date. Interest on Series B Bonds may not exceed the Maximum Rate.

The Series B Bonds will be issuable as fully registered bonds in principal amounts of \$5,000 or any integral multiples thereof.

The Series B Bonds are subject to optional and mandatory sinking fund redemption, and to optional and mandatory tender for purchase, as described herein.

At least 30 days prior to the mandatory tender of the Series B Bonds upon expiration of the Initial Extended Rate Period, the State shall appoint a Remarketing Agent and a Tender Agent, and shall obtain a Liquidity Facility to support the payment of the Purchase Price of tendered Series B Bonds, or shall refund the Series B Bonds on or prior to such tender date. At that time, the State may appoint a different Paying Agent and Registrar for the Series B Bonds.

Mandatory Sinking Fund Redemption

The Series B Bonds shall constitute term bonds subject to mandatory sinking fund redemption and shall be redeemed prior to maturity on March 1 (or, if any such March 1 is not a Business Day, the next succeeding Business Day during an Extended Rate Period) in each of the years and in the respective principal amounts set forth in the table below, and by lot within a maturity, at a redemption price equal to the principal amount to be redeemed, plus accrued interest on such principal amount to the date fixed for redemption.

<u>Year</u>	<u>Amount</u>	<u>Year</u>	<u>Amount</u>	<u>Year</u>	<u>Amount</u>
2013	\$1,890,000	2019	\$2,225,000	2025	\$2,950,000
2014	1,695,000	2020	2,335,000	2026	3,095,000
2015	1,780,000	2021	2,445,000	2027	3,245,000
2016	1,860,000	2022	2,565,000	2028	3,400,000
2017	1,950,000	2023	2,685,000	2029*	3,565,000
2018	2,445,000	2024	2,820,000		

* Final Maturity

Any Series B Bond subject to mandatory redemption may be purchased by the State prior to the thirtieth (30th) day preceding the respective redemption date at a price (including any brokerage and other charges) not exceeding the principal amount thereof, plus accrued interest thereon to the date of redemption.

Optional Redemption

During any period in which interest on the Series B Bonds is determined at Extended Rates (but only during the Initial Extended Rate Period or if the Extended Rate Period is one year in duration), the Series B Bonds are subject to optional redemption prior to their stated maturity at the option of the State in whole or in part on the first Business Day following the last day of the applicable Rate Period, in such amounts and of such maturities (treating sinking fund redemption dates as maturities for such purpose) as the State may direct, at a price equal to the principal amount to be redeemed, without premium, plus the interest accrued on such principal amount to the date fixed for redemption.

Prior to the conversion of Series B Bonds to an Extended Rate Period of more than one year in duration, provisions for the optional redemption of such Series B Bonds to apply to such Series B Bonds during such Extended Rate Period shall be determined by the State. Notice of such redemption provisions shall be included in or with the relevant notice of preliminary Extended Rate as described in Appendix F.

Notice of Redemption

Written notice shall be mailed to registered owners of the Series B Bonds to be redeemed at least fifteen (15) days before the redemption date, at the address that appears on the registration books as of the thirtieth (30th) day preceding the redemption date, but failure to receive any such notice shall not affect the validity of the redemption proceedings. Except for notice of any mandatory sinking fund redemption, any notice of redemption may provide that such redemption is conditional on the availability of sufficient moneys to pay the redemption price, plus interest accrued and unpaid to the redemption date. While DTC or its nominee is the registered owner of the Series B Bonds, the State will give notice of redemption of Series B Bonds to DTC or its nominee or its successor and shall not be responsible for mailing notices of redemption to Direct DTC Participants, to Indirect DTC Participants or to the Beneficial Owners of the Series B Bonds. Any failure of DTC or its nominee or its successor, or of a Direct DTC Participant or Indirect DTC Participant, to notify a Beneficial Owner of a Series B Bond of any redemption will not affect the sufficiency or the validity of the redemption of such Series B Bond. (See Appendix D – “Book-Entry Only System”.) The State can give no assurance that DTC or its successor, the Direct DTC Participants or the Indirect DTC Participants will distribute such redemption notices to the Beneficial Owners of the Series B Bonds, or that they will do so on a timely basis.

Selection of Bonds for Redemption

If less than all of the Series B Bonds shall be called for redemption, the particular Series B Bonds or portions of Series B Bonds to be redeemed shall be selected by lot within a maturity, subject to the following order of priority of redemption: (i) any Provider Bonds; (ii) any Series B Bonds that have been tendered to the Tender Agent on the Redemption Date; and (iii) any other Series B Bonds.

Tenders for Purchase

Optional Tender for Purchase

The Series B Bonds shall be subject to optional tender for purchase by the Owners thereof as described below. As long as the Series B Bonds are in the book-entry only form, demands for purchase may be made by the Beneficial Owners only through such Beneficial Owner's Direct DTC Participant.

While the Series B Bonds bear interest at an Extended Rate, any Series B Bond will be purchased on the demand of the owner thereof on the commencement date of an Extended Rate Period (other than the Extended Rate Conversion Date) at a purchase price equal to the principal amount thereof plus accrued interest, if any, to the Purchase Date, upon written notice to the Tender Agent no later than 5:00 p.m. (New York time) on a Business Day not less than 15 days prior to the commencement of a new Extended Rate Period.

Each notice of tender, must be delivered to the Tender Agent, and must (i) be delivered by the time and date specified above, (ii) state principal amount (or portion thereof) of such Series B Bond to be purchased, (iii) state the Purchase Date on which such Series B Bond is to be purchased, (iv) irrevocably request such purchase, (v) contain the DTC identification number of the Beneficial Owners' Direct DTC Participant and (vi) contain payment instructions. The tendered Series B Bonds must accompany such notice of tender.

Each notice of tender shall automatically constitute (A) an irrevocable offer to sell the principal of the Series B Bond or portion thereof to which the notice relates on the Purchase Date to any purchaser selected by the Remarketing Agent, at the Purchase Price, (B) an irrevocable authorization and instruction to the Paying Agent and Registrar to effect transfer of such Purchase Date, (C) an irrevocable authorization and instruction to the Tender Agent to effect the exchange of the Series B Bond to be purchased in whole or in part for other Series B Bonds of the same maturity in an equal aggregate principal amount so as to facilitate the sale of the principal or portion thereof, and (D) an acknowledgment that such Owner will have no further rights with respect to the principal or interest of the Series B Bond or portion thereof upon payment of the Purchase Price by the Paying Agent and Registrar on the Purchase Date to the Direct DTC Participant from whom the notice of tender is received, except for the right of such Owner to receive such Purchase Price upon surrender of such, Series B Bond to the Tender Agent.

The determination of the Tender Agent as to whether a notice of tender has been properly delivered pursuant to the foregoing shall be conclusive and binding.

Mandatory Tenders for Purchase

The Series B Bonds are subject to mandatory tender for purchase at the Purchase Price on any Variable Rate Conversion Date, upon 15 days mailed written notice, or any Fixed Rate Conversion Date, upon 30 days mailed written notice.

The Series B Bonds also are subject to mandatory tender for purchase at the Purchase Price (i) on a Substitution Date, (ii) on a Business Day which is at least five days prior to the expiration of the Liquidity Facility, or (iii) on a Business Day which is at least five days prior to a Notice Termination Date, in each case upon 30 days mailed written notice.

Payments for Tendered Series B Bonds

Payment of the Purchase Price shall be made before 4:00 p.m., New York City time, on the Purchase Date and upon receipt by the Paying Agent and Registrar of 100% of the aggregate Purchase Price of the tendered Series B Bonds, the Paying Agent and Registrar shall pay the Purchase Price of such Series Bonds to the Owners thereof (unless otherwise directed in the notice of the tender) at its principal office or, if requested, by bank wire transfer. Such payments shall be

made in immediately available funds. See “Insufficient Funds for Purchase” below for a description of applicable procedures when the Paying Agent and Registrar does not receive 100% of the aggregate Purchase Price of the tendered Series B Bonds.

Payments of such Purchase Price are to be made from the following sources in the order of priority indicated: (i) the proceeds of the sale of the Series B Bonds which have been remarketed by the Remarketing Agent (other than proceeds of a sale of the Series B Bonds to the State); and (ii) the proceeds of the sale of the Series B Bonds which have been purchased by the Liquidity Provider pursuant to the Liquidity Facility or other proceeds received under or pursuant to a Liquidity Facility; and (iii) moneys paid by the State for such purpose. **The State shall not be obligated to provide funds for the payment of the Purchase Price of Series B Bonds upon any tender.**

Delivery of Bonds; Effect of Failure to Surrender

All Series B Bonds to be purchased on any mandatory tender date shall be required to be delivered to the Tender Agent on or before 11:30 a.m., New York City time, on the Purchase Date. As described above, in the event of an optional tender for purchase, the tendered Series B Bonds must accompany the notice of tender.

If the Owner of any Series B Bond (or portion thereof) that is subject to purchase fails to surrender such Series B Bond to the Tender Agent for purchase when required, and if the Paying Agent and Registrar is in receipt of the Purchase Price therefore, such Series B Bond (or portion thereof) shall nevertheless be deemed purchased on the Purchase Date and ownership of such Series B Bond (or portion thereof) shall be transferred to the purchaser thereof as provided in the Resolution. Any Owner who fails to deliver a Series B Bond for purchase as required above shall have no further rights thereunder except the right to receive the Purchase Price thereof upon presentation and surrender of said Series B Bond to the Tender Agent.

Insufficient Funds for Purchases

If the moneys available for purchase of Series B Bonds are inadequate for the purchase of all Series B Bonds which are tendered on any Purchase Date, the interest thereon subject to such purchase shall be determined at a rate which is the lesser of (i) a rate established by the Remarketing Agent or (ii) the Maximum Rate, to the date on which the earliest of the following occurs:

- (a) The Fixed Rate Conversion Date, or the Conversion Date for any other Rate Period if a Liquidity Facility is in place pursuant to the Resolution;
- (b) The date on which any default by the Liquidity Provider under the terms of the Liquidity Facility has been cured; or
- (c) The effective date of a new interest rate established by the Remarketing Agent which is less than the Maximum Rate after the date on which an Alternate Liquidity Facility meeting the requirements of the Resolution becomes effective

If the preceding provisions become applicable, (i) the Tender Agent shall immediately (but no later than the end of the next succeeding Business Day) return all tendered Series B Bonds to the Owners thereof and notify all Owners of Series B Bonds in writing of the rate at which the interest thereon will be determined pursuant to the preceding provisions and (ii) the Paying Agent and Registrar shall return all moneys received for the purchase of such Series B Bonds to the Persons who provided moneys; provided, however, that the Owners shall retain all rights to tender the Series B Bonds pursuant to the provisions of the Resolution and the obligation of the State to honor such tenders shall remain in effect until payment therefore has been provided in accordance with the provisions of the Resolution. **Notwithstanding the foregoing, the State shall not be obligated to provide funds for the payment of the Purchase Price of Series B Bonds upon any tender.**

Conversion of Series B Bonds to Other Rate Periods

The Series B Bonds may be converted to different Variable Rate Periods or to a Fixed Rate Period upon the terms and conditions and at the times described in Appendix F hereto. The Series B Bonds may only be converted to a different Variable Rate Period or to a Fixed Rate Period on an Interest Payment Date on which a new Extended Rate Period would otherwise have commenced.

Liquidity Facility

At all times during any Variable Rate Period, the State shall cause a Liquidity Facility to be provided to the Paying Agent and Registrar for the benefit of the Series B Bondholders; provided, however, that no Liquidity Facility shall be required (i) during any Extended Rate Period prior to thirty (30) days before any date on which an Owner may, at such Owner's option, tender Series B Bonds for purchase or (ii) in any Rate Period during which the Series B Bonds receive a rating from each Rating Agency in the highest short term category (without regard to gradations with such category), which rating is not based on a Liquidity Facility; and provided further, however, that the suspension of a Liquidity Facility shall not be deemed a failure to provide a Liquidity Facility. As provided by the Resolution, the State shall obtain a Liquidity Facility before the tender date, if any, for which the same may be required, but in any case (if required) no later than thirty (30) days prior to the applicable tender date, or shall refund such Series B Bonds on or before such tender date.

Each Liquidity Facility (i) shall consist of a letter of credit, line of credit, standby bond purchase agreement or similar agreement, (ii) shall provide for the purchase of all or a portion of the Bonds during a Variable Rate Period, (iii) shall be delivered by (A) a financial institution which has a long term debt rating of at least "A" from Fitch, "A2" from Moody's or A from S&P, and a short term debt rating of at least "F-1" by Fitch, "VMIG-1" by Moody's or SP-1 from S&P, respectively, or such other comparable rating by such or any other Rating Agency, in each case if they are providing a rating on outstanding Bonds, or (B) the Tennessee Consolidated Retirement System, and (iv) shall provide for cancellation in connection with replacement by an Alternate Liquidity Facility not less than 5 days after the Substitution Date.

Any Liquidity Facility may provide for termination thereof as a result of an Event of Termination. If such termination is permitted, the date upon which the Liquidity Facility is to terminate (the Notice Termination Date) must be at least thirty (30) days after the date on which the Paying Agent and Registrar, Remarketing Agent and Tender Agent receive notice from the Liquidity Provider stating that as a result of an Event of Termination under the Liquidity Facility, the Liquidity Provider in accordance with the provisions of the Liquidity Facility has elected to terminate the Liquidity Facility and stating the date of termination. Furthermore, each such notice must be received on a Business Day and any notice received after 11:30 a.m., New York City time, on a Business Day shall be deemed to have been received on the next Business Day.

The Resolution provides that the Paying Agent and Registrar shall not consent to or permit any amendment or modification of a Liquidity Facility or any credit or reimbursement agreement pursuant to which a Liquidity Facility has been issued which would materially adversely affect the rights or interests of the Owners of any of the Series B Bonds without the written consent of the Owners of 100% in aggregate amount of the Series B Bonds, unless such amendment or modification shall take place simultaneously with a remarketing of all of the Series B Bonds and the purchasers of the remarketed Series B Bonds shall have had notice of such amendment or modification.

If the State proposes to provide an Alternate Liquidity Facility, in substitution for any Liquidity Facility then in effect, the Paying Agent and Registrar shall send to the Series B Bondholders notice thereof not later than 20 calendar days prior to the proposed Substitution Date. The Paying Agent and Registrar shall not accept such Alternate Liquidity Facility unless the Paying Agent and Registrar shall have received at the time of delivery of the Alternate Liquidity Facility, (A) a certificate from an Authorized Officer and a written acknowledgement by the Liquidity Provider stating that all amounts owing to the Liquidity Provider under the Liquidity Facility or any other reimbursement or similar agreement pursuant to which the Liquidity Facility to be replaced has been issued have been paid and that there are no Provider Bonds outstanding or that all Provider Bonds have been purchased by the Alternate Liquidity Facility and (B) a letter from each Rating Agency confirming a rating of the Series B Bonds upon the effective date of such Alternate Liquidity Facility.

Paying Agent and Registrar

The State (acting through its State Treasurer or State Comptroller or both) currently is the Paying Agent and Registrar for the Bonds. The State may at any time appoint a different Paying Agent and Registrar for either or both series of Bonds.

Book-Entry Only System

Upon initial issuance, the Bonds will be available only in book-entry form. The Depository Trust Company ("DTC"), New York, New York, will act as securities depository for the Bonds. The ownership of one fully registered Bond

for each maturity of each series, each in the aggregate principal amount of such maturity, will be registered in the name of Cede & Co. (DTC's partnership nominee) and deposited with DTC. Beneficial owners of Bonds will not receive physical delivery of bond certificates, except under limited circumstances.

In addition, tenders of Series B Bonds will be effected only through DTC's book-entry only system.

For a description of DTC and its book-entry only system, see "Appendix D – Book-Entry Only System".

PLAN OF REFUNDING AND APPLICATION OF BOND PROCEEDS

The Bonds are being issued to refund the series (or portions thereof) and maturities of general obligation bonds of the State (collectively, the "Refunded Bonds") set forth below:

- General Obligation Bonds, 1997 Series B, dated May 1, 1997, maturing on May 1, 2005 through May 1, 2027, both inclusive, currently outstanding in the aggregate principal amount of \$22,670,000 (the "Refunded 1997 Bonds"). The Refunded 1997 Bonds initially will be refunded to maturity or, in the case of Refunded 1997 Bonds maturing in 2023 and 2027, their earlier mandatory sinking fund redemption dates. However, **the State reserves the right to call the Refunded 1997 Bonds on or after May 1, 2007**, at any time as a whole or in part from time to time in any order of maturity determined by the State and by lot within a maturity, at the redemption prices (expressed as percentages of the principal amount to be redeemed), plus accrued interest on such principal amount to the date fixed for redemption, as follow:

Period During Which Redeemed (both dates inclusive)	Redemption Price
May 1, 2007 through April 30, 2008	101½%
May 1, 2008 through April 30, 2009	101%
May 1, 2009 through April 30, 2010	100½%
May 1, 2010 and thereafter	100%

- General Obligation Bonds, 1998 Series A, dated May 1, 1998 maturing on May 1, 2005 through May 1, 2018, both inclusive, in the aggregate principal amount of \$8,125,000 (the "Refunded 1998 Bonds") as follows:

Maturity <u>May 1</u>	Outstanding Principal <u>Amount</u>	Principal Amount To Be <u>Refunded</u>
2005	\$5,950,000	\$ 420,000
2006	5,970,000	440,000
2007	5,990,000	460,000
2008	6,010,000	480,000
2009	6,040,000	510,000
2010	6,060,000	530,000
2011	6,085,000	555,000
2012	6,115,000	585,000
2013	6,140,000	610,000
2014	6,170,000	640,000
2015	6,205,000	675,000
2016	6,235,000	705,000
2017	6,270,000	740,000
2018	6,310,000	<u>775,000</u>
		<u>\$8,125,000</u>

The Refunded 1998 Bonds initially will be refunded to maturity. However, **the State reserves the right to call the Refunded 1998 Bonds on or after May 1, 2008**, at any time as a whole or in part from time to time in any order of

maturity determined by the State and by lot within a maturity, at the redemption prices (expressed as percentages of the principal amount to be redeemed), plus accrued interest on such principal amount to the date fixed for redemption, as follows:

Period During Which Redeemed (both dates inclusive)	Redemption Price
May 1, 2008 through April 30, 2009	101%
May 1, 2009 and thereafter	100%

- General Obligation Bonds, 1999 Series C, dated June 1, 1999, maturing on May 1, 2008, May 1, 2013, and May 1, 2018 through May 1, 2029, both inclusive, currently outstanding in the aggregate principal amount of \$19,080,000 (the "Refunded 1999 Bonds"). The Refunded 1999 Bonds maturing on May 1, 2008 and May 1, 2013, will be refunded to maturity. The Refunded 1999 Bonds maturing on and after May 1, 2018, will be called for redemption on May 1, 2013, at a redemption price of par, plus accrued interest, if any, to the date fixed for redemption. Such designation for redemption will be irrevocable upon issuance of the Bonds.

Written notice of any such redemption shall be mailed to the registered owners of the Bonds to be redeemed at least thirty (30) days before the redemption date. While DTC or its nominee is the registered owner of the Refunded Bonds, the State or the Refunding Trustee (described below) shall not be responsible for mailing notices of redemption to Direct DTC Participants or Indirect DTC Participants or to the Beneficial Owners of the Refunded Bonds.

The proceeds of the Bonds and other available moneys will be used to acquire direct general obligations of or obligations the payment of principal of and interest on which are unconditionally guaranteed by the United States of America (the Government Obligations") and to pay certain costs of issuance. The Government Obligations and the interest earned thereon will be sufficient, and will be used, together with other available moneys, to pay (i) the principal of and redemption premiums, if any, on the Refunded Bonds on the respective redemption dates described above and (ii) the principal of and interest on the Refunded Bonds due on and prior to such redemption dates. The Government Obligations will be purchased from the Treasury Department of the United States of America or in the open market through a competitive bidding process. If such securities are purchased in the open market, they may be so purchased from Underwriters of the Bonds.

Deutsche Bank National Trust Company has been appointed Refunding Trustee and will enter into a Refunding Trust Agreement with the State Funding Board. The Government Obligations and other available moneys will be irrevocably deposited with the Refunding Trustee in a Refunding Trust Fund and irrevocably set aside for the benefit of the holders of the Refunded Bonds. The State will obtain verification of sufficiency of the Refunding Trust Fund from McGladrey & Pullen LLP, a firm of independent certified public accountants (See "Verification Agent").

The proceeds of the Bonds and other available funds are expected to be applied on the date of issue of the Bonds in the estimated amounts as follows:

Sources and Uses of Funds

Sources of Funds:

Par Amount Series A.....	\$11,885,000.00
Par Amount Series B.....	42,950,000.00
Accrued Interest.....	253,715.85
Other Available Funds.....	<u>696,779.52</u>
Total.....	<u>\$55,785,495.37</u>

Uses of Funds:

Deposit to Refunding Trust Fund for Refunded Bonds.....	\$55,295,774.23
Costs of Issuance.....	295,250.00
Underwriters' Discount	<u>194,471.14</u>
Total.....	<u>\$55,785,495.37</u>

SECURITY FOR THE BONDS

All general obligation bonds of the State, including the Bonds, are and will be direct general obligations of the State, payable as to both principal and interest from any funds or moneys of the State from whatever source derived. The full faith and credit of the State is pledged to the payment of principal of and interest on all general obligation bonds. As additional security to support its general obligation bonds, including the Bonds and tax revenue anticipation notes, the State, pursuant to Section 9-9-103, Tennessee Code Annotated, has pledged (i) the annual proceeds of a tax of up to five cents per gallon upon gasoline; (ii) the annual proceeds of a special tax of one cent (1¢) per gallon on petroleum products; (iii) one-half of the annual proceeds of motor vehicle registration fees now or hereafter required to be paid to the State; and (iv) the annual proceeds of the franchise taxes imposed by the franchise tax law of the State (collectively, "Special Taxes"). All general obligation bonds and tax revenue anticipation notes share this pledge of Special Taxes on a pro rata basis.

The Special Taxes collected for the last three fiscal years, as reported for each year in the June monthly Statement of Revenue Collections (prepared on a cash basis), were as follows (amounts have been rounded):

	Fiscal Year Ended		
	<u>June 30, 2003</u>	<u>June 30, 2002</u>	<u>June 30, 2001</u>
Gasoline Tax	\$149,583,000	\$144,722,000	140,917,000
Special Petroleum Tax	43,752,000	44,081,000	44,286,000
One-half of Motor Vehicle Registration Fees	108,822,000	105,816,000	101,727,000
Franchise Taxes	<u>489,579,000</u>	<u>420,768,000</u>	<u>480,242,000</u>
Total	<u>\$791,736,000</u>	<u>\$715,387,000</u>	<u>\$767,172,000</u>

Source: Department of Revenue

Pursuant to Section 9-9-106, Tennessee Code Annotated, the Funding Board has a lien on the taxes, fees and revenues from the Special Taxes in the full amount required to pay principal of and interest on the State's general obligation bonds and tax revenue anticipation notes issued under Title 9, Chapter 9, Tennessee Code Annotated. Pursuant to Section 9-9-111, Tennessee Code Annotated, the State has covenanted not to decrease by legislative action the Special Taxes unless the Funding Board certifies that the State is not in default in the payment of any outstanding debt and that Special Taxes at lower rates specified by the Funding Board in such year or years (not to exceed two (2) years) will be sufficient to make all payments required to be made therefrom by the State on all of its obligations during the period that such decrease will be in effect.

The principal amount of general obligation bonds and tax revenue anticipation notes that the State may issue is limited by Section 9-9-104, Tennessee Code Annotated, which provides in part as follows:

[N]o bonds or other obligations will be made a charge upon the special revenues consisting of the proceeds of the gasoline tax, franchise tax, the special tax on petroleum products provided for by Section 67-3-1303 and motor vehicle registration fees pledged under the provisions of this chapter, in addition to the obligations and charges authorized by this chapter, unless the revenues pledged by Section 9-9-103 or the aggregate of the pledged gasoline tax, the special tax on petroleum products provided for by Section 67-3-1303, motor vehicle registration fees and one-third of the entire annual proceeds of franchise and excise taxes imposed by the franchise and excise tax laws compiled in Title 67, Chapter 4, parts 9 and 8 (now parts 21 and 20), whichever sum is lower, for the last preceding fiscal year shall have aggregated not less than one hundred and fifty percent (150%) of the amount necessary to pay the annual interest upon all outstanding obligations and charges, for the payment of which such revenues are pledged, and the annual interest upon the obligations then proposed to be issued, together with the annual amount necessary for the amortization of said outstanding obligations and charges and the obligations then proposed to be issued; provided, however, in determining said outstanding obligations and charges there shall be excluded any outstanding bonds with respect to which refunding bonds have been issued and sold and the proceeds of which are to be applied to retire said outstanding bonds.

The amount of Special Taxes collected for the fiscal year ended June 30, 2003 was \$791,736,000. The aggregate of the pledged gasoline tax, the special tax on petroleum products, motor vehicle registration fees and one-third of the entire

annual proceeds of franchise and excise taxes collected for the fiscal year ended June 30, 2003 was \$669,665,000. Pursuant to Section 9-9-104, Tennessee Code Annotated, the debt service limit is obtained by dividing the lesser amount (\$669,665,000) by one-point-five (1.5). Therefore, the debt service limit for the fiscal year ending June 30, 2004 is \$446,443,333. The greatest amount of principal and interest payable in any fiscal year on outstanding bonds for the payment of which Special Taxes have been pledged, including the Bonds (for the Series B Bonds at a rate of 4.82% to March 1, 2029) and excluding the Refunded Bonds and CP, is not more than \$155,061,836. Even if the maximum variable interest rate (12%) is applied to the Series B Bonds, the greatest amount of principal and interest payable in any fiscal year remains \$155,061,836.

Section 67-6-103(a)(5), Tennessee Code Annotated, currently provides that 0.9185% of the sales and use tax collections is appropriated to the Funding Board for the payment of principal of and interest on the State's general obligation bonds, but not tax revenue anticipation notes. This statutory provision subsequently may be changed or eliminated. The total sales and use tax collections and the amounts allocated to debt service for the last three fiscal years as reported in the State's Annual Financial Reports (prepared on a modified accrual basis) were as follows:

	<u>Total Collections</u>	<u>Allocation to Debt Service</u>
June 30, 2003	\$5,459,444,000	\$39,069,000
June 30, 2002	\$4,647,768,000	\$38,449,000
June 30, 2001	\$4,643,337,000	\$38,480,000

For a discussion of projected current year collections, see "State Finances – Financial Information and Budget Summary for Fiscal Years 2003-2004 and 2004-2005".

All general obligation indebtedness of the State is on parity and shares pro rata with all other general obligation indebtedness of the State, except that the Special Taxes secure only general obligation bonds and tax revenue anticipation notes. The State is permitted by the State Constitution to levy ad valorem taxes on all of the taxable property within the State for the payment of the principal of and interest on the State's general obligation indebtedness; however, the State does not currently levy such a tax.

For a table of annual debt service requirements for all general obligation bonds, excluding the Bonds, see "State Indebtedness – Outstanding General Obligation Bonded Indebtedness". In addition, the State may issue, and currently is issuing as CP, general obligation bond anticipation notes for the payment of which the full faith and credit of the State, but not Special Taxes, is pledged. (See "State Indebtedness – Commercial Paper Program".) In addition, the State is authorized to issue general obligation tax revenue anticipation notes for the payment of which the full faith and credit of the State, and Special Taxes, are pledged. (See "State Indebtedness – Tax Revenue Anticipation Notes".)

Remedies and Rights of Bondholders

Each Bond when duly issued will constitute a contract between the State and the registered owner of the Bond. If the State defaults in payment of any State obligation to which Special Taxes are pledged and/or other fees and taxes are pledged for this purpose, State law requires the State Treasurer or other appropriate authority to pay the amount required for the payment of such obligations out of the first monies received from such taxes and fees. Under State law, a holder or purchaser of any such obligation, including the Bonds, has a vested right in the performance of the covenants and pledges made by the State in the issuance of such obligations and may enforce by appropriate proceedings such covenants, pledges, and duties imposed on any State agency or officer in connection with the issuance of such obligations. The State has not generally waived immunity from suit or extended its consent to be sued and this may bar actions against such agencies and officers. Current State law provides that monetary claims against the State for breach of its contractual obligations and certain other causes may be heard and determined exclusively in the forum of the Tennessee Claims Commission, an administrative tribunal, where the State may be liable only for actual damages and certain costs.

Under the State Constitution, public money may be expended only pursuant to appropriations made by law, (See "State Finances.") Such expenditures include, but are not limited to, the payment of debt service and funding any judgment in the Tennessee Claims Commission. Continuing appropriations exist for the payment of debt service on the State's general obligation bonds, including the Bonds, from Special Taxes, in connection with the pledge of Special Taxes in Title 9, Chapter

9, Tennessee Code Annotated, and under current law, from a specified percentage of sales and use taxes as discussed above. Furthermore, 2001 Pub Ch. 264 amends Section 9-9-103, Tennessee Code Annotated, by appropriating to the State Funding Board on a direct and continuing basis a sum sufficient for payment of debt service (principal, interest and premium, if any) on outstanding general obligation bonds and other debt obligations (including notes) from any funds held in the State treasury not otherwise legally restricted, independent of an appropriation bill otherwise required by State law. Whether a continuing appropriation exists for the payment of a claim in the Tennessee Claims Commission for unpaid debt service is not clear, and in any event sovereign immunity and other legal principles may bar actions to compel the General Assembly to appropriate moneys for such payments.

STATE INDEBTEDNESS

General

The State Constitution forbids the expenditure of the proceeds of any debt obligation for a purpose other than the purpose for which it was authorized. Under State law, the term of bonds authorized and issued cannot exceed the expected life of the projects being financed. Furthermore, the amount of bonds issued cannot exceed the amount authorized by the General Assembly.

The procedure for funding State debt is provided by Chapter 9 of Title 9, Tennessee Code Annotated. The Funding Board of the State of Tennessee is the entity authorized to issue general obligation indebtedness of the State. The Funding Board is composed of the Governor, the State Comptroller of the Treasury, the Secretary of State, the State Treasurer, and the Commissioner of Finance and Administration. The Funding Board issues all general obligation indebtedness in the name of the State pursuant to authorization by the General Assembly without concurrence or approval by any other governmental agency or by the electorate. Although the Funding Board determines the terms of general obligation indebtedness, the interest rate on the general obligation indebtedness cannot exceed the State Formula Rate which is set forth in Section 47-14-103, Tennessee Code Annotated.

Bonds by Purpose

State law provides that the State may issue general obligation bonds or notes for one or more purposes, whether or not the purposes were authorized in the same legislative act. As of May 31, 2004, the State had \$1,138,335,000 (unaudited) of general obligation bonds outstanding, of which \$8,020,000 was for public health loans, and the remaining \$1,130,315,000 was for general governmental purposes. The bonds for the public health loans were initially issued in the amount of \$85,195,000 to fund loans to local government units to aid in constructing and improving sewage treatment works, waterworks construction, and solid waste resource recovery facilities. State law requires local governments receiving loans to repay the State through scheduled repayments sufficient to pay indebtedness incurred by the State to finance such loans. Consequently, it is not anticipated that any State tax revenues will be required to meet the principal of or interest on the public health loan bonds. Since 1978, public health loans have been funded through the issuance of revenue bonds and notes by the Tennessee Local Development Authority. (See “Debt of Certain Agencies and Authorities – The Tennessee Local Development Authority”).

Commercial Paper Program

Bond anticipation notes (the “Notes”) may be issued for purposes for which bonds have been authorized, if the notes are also authorized by legislative act. Notes have been authorized to be issued for the purposes of all existing bond authorizations.

In March 2000, the State instituted a general obligation commercial paper program for authorized capital projects. CP will be issued under the Commercial Paper Resolution, adopted by the members of the Funding Board of the State on March 6, 2000, in a principal amount outstanding at any one time not to exceed \$250,000,000. The CP constitute Notes and are direct general obligations of the State for the payment of which, as to both principal and interest, the full faith and credit of the State, but not Special Taxes, are pledged.

The State has entered into a Standby Commercial Paper Purchase Agreement with the Tennessee Consolidated Retirement System (“TCRS”) under which TCRS is obligated to purchase newly issued CP issued to pay the principal of

other CP, subject to suspension or termination upon the occurrence of certain events. If and for so long as TCRS is the Standby Purchaser, the principal amount of CP maturing on any day shall not exceed \$50,000,000 or such greater principal amount as it may agree to.

The CP will have varying maturities of not more than 270 days from their respective dates of issuance; provided, however, that no CP may mature later than the sixth business day prior to the stated expiration date without regard to any early termination of the Liquidity Facility. Currently, this date is April 1, 2005. CP is not subject to redemption prior to maturity.

As of May 31, 2004, \$72,775,000 (unaudited) principal amount of CP was outstanding under this program.

Tax Revenue Anticipation Notes

The State is authorized to issue general obligation tax revenue anticipation notes ("TRANS") in anticipation of the receipt of tax revenues in the then current fiscal year of the State. TRANS, if issued, will constitute direct obligations of the State for the payment of which, as to both principal and interest, the full faith and credit of the State, and also Special Taxes, are pledged. All TRANS must be paid in the same fiscal year in which they are issued. The State has not heretofore issued TRANS.

Outstanding General Obligation Bonded Indebtedness

As of May 31, 2004, there were \$1,138,335,000 (unaudited) State general obligation bonds outstanding, excluding the Bonds

The annual debt service requirements for the outstanding long-term general obligation bonded indebtedness (including the Bonds and excluding the Refunded Bonds) are as follows:

Fiscal Year	Principal	Interest*	Total	Fiscal Year	Principal	Interest*	Total
2005	\$98,890,000	\$56,171,836	\$155,061,836	2018	\$39,775,000	\$8,589,331	\$48,364,331
2006	96,940,000	51,739,775	148,679,775	2019	30,560,000	6,559,240	37,119,240
2007	85,975,000	46,835,066	132,810,066	2020	26,785,000	5,004,158	31,789,158
2008	80,355,000	42,697,728	123,052,728	2021	19,405,000	3,645,700	23,050,700
2009	79,955,000	38,889,798	118,844,798	2022	19,535,000	2,679,250	22,214,250
2010	77,405,000	35,059,825	112,464,825	2023	11,460,000	1,705,910	13,165,910
2011	76,305,000	31,243,147	107,548,147	2024	11,485,000	1,149,824	12,634,824
2012	72,570,000	27,421,243	99,991,243	2025	3,140,000	797,504	3,937,504
2013	72,775,000	23,746,224	96,521,224	2026	3,295,000	646,051	3,941,051
2014	66,600,000	20,064,011	86,664,011	2027	3,245,000	492,122	3,737,122
2015	58,515,000	16,694,969	75,209,969	2028	3,400,000	335,713	3,735,713
2016	53,455,000	13,726,586	67,181,586	2029	<u>3,565,000</u>	<u>171,833</u>	<u>3,736,833</u>
2017	47,905,000	11,024,690	58,929,690				
				Totals	<u>\$1,143,295,000</u>	<u>\$447,091,534</u>	<u>\$1,590,386,534</u>

* For purposes of this schedule, the interest on Series B Bonds is calculated using 4.82% through 2029 in accordance with GASB 38, which states that interest requirements for variable-rate debt should be determined using the rate in effect at the financial statement date. Different interest rates may apply to the Series B Bonds commencing March 1, 2010, which rates cannot exceed the maximum rate of 12%.

The State had authorized, as of June 15, 2004, \$1,570,994,785 (unaudited) of general obligation bonds that had not been issued.

STATE FINANCES

The Budget Process

The State budget originates in the executive branch with the Governor's annual budget recommendation to the General Assembly. Initially, budget preparation instructions are issued by the Department of Finance and Administration to all State agencies and departments. These instructions describe the Administration's guidelines related to continuing the current level of service (baseline budget) and proposed budget improvements. The instructions are to be used by agencies and departments in preparing their budgets for submission to the Department of Finance and Administration in October of each year.

During the fall, each department's budget request is reviewed, and improvement requests are analyzed by the Department of Finance and Administration. Conferences are held with departmental and agency representatives, the Director of Budget, and the Department of Finance and Administration staff to determine which, if any, of the proposals should be recommended.

Under State law, the Governor submits the recommended budget to the General Assembly at the start of the legislative session. The budget document must be presented to the General Assembly prior to February 1 of each year, except that a Governor in the first year of a four-year term of office must present a budget prior to March 1 of that year. However, the General Assembly may extend these deadlines by joint resolution. Subsequently, the Governor submits a General Appropriation Bill and bond authorization bills containing appropriations and general obligation bond authorizations required to finance the program levels and capital outlay proposed in the Governor's budget. Throughout the legislative session, the Finance, Ways and Means Committees and appropriate standing committees of the House and Senate hold budget hearings for each department to determine if changes should be made to the proposals.

During the 1997 legislative session, the Office of Legislative Budget Analysis was created to enable the General Assembly to strengthen its expertise in governmental budgeting and financing and in making public policy decisions. The office was created as an independent department of the legislature working for both the Senate and the House of Representatives charged with reviewing and analyzing the State's budget and overall financial condition. The staff summarizes and analyzes the Governor's budget proposal for members of the General Assembly, secures budget justification data from the various state agencies, provides recommendations on budget proposals and provides assistance on financial matters to the standing committees, as directed.

Under the State Constitution, money may be drawn from the Treasury only through an appropriation made by law. The primary source of the annual expenditure authorization is the General Appropriation Act as approved by the General Assembly and signed by the Governor. These appropriations are generally limited to a one-year period of availability. The General Appropriation Act requires a simple majority vote of each House of the General Assembly. Approval of the General Appropriation Bill usually occurs during the last week of the legislative session. Once signed by the speaker of each House of the General Assembly, the General Appropriation Act is sent to the Governor for signature. If the Governor does not act within ten days, excluding Sundays, the General Appropriation Act becomes law without signature. The Governor may reduce or eliminate specific line items in the General Appropriation Act or any other appropriations bill without vetoing the entire bill. Such individual line-item vetoes are subject to override by a vote of a majority of the members elected to each House of the General Assembly.

Appropriations also may be included in legislation other than the General Appropriation Act. The individual bills containing appropriations must be heard by the Finance, Ways and Means Committee, and may be heard by the relevant standing committee, in each House of the General Assembly. After all related committees recommend passage, bills containing appropriations must be approved by a majority vote in each House of the General Assembly and be acted upon by the Governor. Bills of this character are also subject to reduction or elimination by individual line-item veto by the Governor and override by the General Assembly, as described above.

Funds necessary to meet an appropriation need not be in the Treasury at the time such appropriation is enacted; revenues may be appropriated in anticipation of their receipt.

Development of Revenue Estimates

The development of the general fund revenue estimates begins with a forecast of national economic activity for the State budget period. The State currently contracts with The University of Tennessee Center for Business and Economic Research (“UT-CBER”) to prepare an annual Economic Report to the Governor containing short-term business cycle-sensitive forecasts as well as longer-term or trend forecasts for the year and to prepare quarterly updates throughout the year. UT-CBER subscribes to the macroeconomic forecasting services of Wharton Econometric Forecasting Associates. The Wharton National Economic Forecast becomes the principal input to the Tennessee Econometric Model which is utilized to develop a forecast of similar indicators of in-state activity.

At least annually, the Funding Board secures from UT-CBER the estimated rate of growth of the State’s economy as measured by the forecast change in Tennessee personal income. The Funding Board reviews the estimated rate of growth in Tennessee personal income and reports to the General Assembly its comments relating to the reasonableness of the estimate, including any different estimate deemed necessary.

The Funding Board is further directed by statute to conduct public hearings to develop consensus ranges of estimates of State revenue for the current fiscal year and the next succeeding fiscal year. At the hearings representatives of state higher education institution business centers, including UT-CBER, present revenue estimates and economic forecasts. On December 1, or as soon thereafter as practical, the Funding Board presents its consensus ranges of State revenue estimates, and a summary of the economic forecast on which the estimates are based, to the Governor and the Chairs of the Senate and House Finance, Ways and Means Committees. Although not mandated prior to final legislative action on the budget, the Funding Board receives updated estimates and forecasts at public hearings in the spring and forwards any revision to prior estimates and the reasons therefor to the Governor and Chairs. The Commissioner of Finance and Administration has the responsibility for preparing the revenue estimates presented in the budget document.

Reserve for Revenue Fluctuations

In 1996, the General Assembly enacted legislation determining the allocation goal for the reserve to be five percent of estimated State tax revenues to be allocated to the general fund and education trust fund. Beginning with the budget for the fiscal year 1998-99 and until this funding level is achieved, the Governor is to budget an allocation to the reserve in an amount at least equal to ten percent of the estimated growth in estimated State tax revenues to be allocated to the general fund and education trust fund. Amounts in the revenue fluctuation reserve may be utilized to meet State tax revenue shortfalls. An amount not to exceed the greater of \$100 million or one-half of the amount in the reserve may be utilized to meet expenditure requirements in excess of budgeted appropriation levels. Use of the reserve for expenditure requirements requires prior notice to and meetings of the Senate and House Finance, Ways and Means Committees. The reserve amount was established as \$101.4 million for fiscal years 1993-94 through 1997-98. It was increased to \$127 million for fiscal year 1998-99, to \$165.1 for fiscal year 1999-2000, and to \$178 million on June 30, 2001, on June 30, 2002 and on June 30, 2003. The Appropriations Act, as amended, increases the reserve fund to \$217 million on June 30, 2004. The reserve fund is budgeted to increase to \$273.4 million at June 30, 2005. See “State Finances - Financial Information and Budget Summary for Fiscal Years 2003-2004 and 2004-2005)” for a discussion of possible utilization of this fund in the current and next fiscal years.

Financial Control Procedures

The State Constitution requires, for current operations, expenditures for any fiscal year not to exceed the State’s revenues and reserves, including the proceeds of any debt obligation, for that year. The State Constitution prohibits the issuance of debt for operating purposes maturing beyond the end of a fiscal year. State law permits tax anticipation borrowing but any amount borrowed must be repaid by the end of the fiscal year.

Generally, the executive branch controls the expenditure of State funds for the operation of State government. Two important concepts are involved in the execution of the General Appropriation Act: preparation of work programs and development of allotment controls. Analysts of the Division of Budget, Department of Finance and Administration, and fiscal personnel in the various State departments and agencies have the responsibility of reconciling the General Appropriation Act, as approved, with the submitted budget. State law requires that administrative agencies prepare a work program for each fiscal year. These work programs indicate separate annual spending requirements for payroll and other operating expenses necessary to carry out agency programs. The head of any agency may revise the work program during the fiscal year because of changed conditions and submit such revision for approval. If the Commissioner of Finance and Administration and the

Governor approve the revision, then the same procedure for review, approval and control is followed as in making the original allotments. The aggregate of all allotments after the revision cannot exceed the total appropriations made to the agency for the fiscal year in question.

All expenditures of State administrative agencies are processed through the Department of Finance and Administration and are measured against work program allotments. Savings which may occur as a result of the difference between the amounts provided in the work program allotments for payroll and other operating expenditures and the amounts actually spent for those expenditures accumulate throughout the fiscal year unless a work program is revised to re-allot unspent amounts. Likewise, departmental revenue surpluses cannot be spent until approved by the Commissioner of Finance and Administration and, in some cases, reviewed by the Finance, Ways and Means Committees of the General Assembly. Such central spending control offers executive flexibility relative to any anticipated surplus or shortfall in the budget.

The Governor may effect spending reductions to offset unforeseen revenue shortfalls or unanticipated expenditure requirements for particular programs. These spending reductions can take the form of deferred equipment purchases, hiring freezes, and similar cutbacks. If necessary, the Governor may reduce portions of administrative budgets prior to allotment. Furthermore, the Governor is authorized to call special sessions of the General Assembly at any time to address financial or other emergencies.

Financial Information and Budget Summary for Fiscal Years 2003-2004 and 2004-2005

Financial Information

The General Assembly approved an annual appropriations act on May 29, 2003 for fiscal year 2003-2004. The 2003-2004 budget is balanced with recurring revenue supporting recurring expenditures.

On an accrual basis, current revenue exceeds budgeted estimates. For the ten months ending May 31, 2004, the State's General Fund is \$254.3 million over budgeted estimates and the four other funds (the Highway Fund, Sinking Fund, City and County Fund and Earmarked Fund) are over budgeted estimates by \$22.9 million. Therefore, overall revenues are \$277.2 million over budgeted estimates. All numbers are unaudited.

The General Assembly passed, and on June 15, 2004 the Governor signed, the Appropriations Bill for the fiscal year 2004-2005 budget. The 2004-2005 budget, as passed by the General Assembly and signed by the Governor, is balanced with recurring revenues supporting recurring expenditures.

Revenue Growth

At the State Funding Board meeting held on April 19, 2004 the Board made the following consensus revenue growth projections:

	Fiscal Year 2003-2004		Fiscal Year 2004-2005	
	<u>Low</u>	<u>High</u>	<u>Low</u>	<u>High</u>
Total State Taxes	5.50%	6.05%	3.60%	4.35%
General Fund Only	6.60%	7.35%	3.85%	4.60%

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Budget Summary

The following tables compare sources and uses of funds for fiscal years 2003-2004 and 2004-2005:

	Estimated Budget FY 2003-2004	Preliminary Budget FY 2004-2005	Difference
Tax Revenue			
Sales and Use Taxes	\$ 5,787,300,000	\$ 6,096,600,000	\$ 309,300,000
Other Taxes	3,220,800,000	3,298,900,000	78,100,000
Other Miscellaneous Revenues	837,231,800	842,809,600	5,577,800
Federal Funds	8,700,000,000	9,200,000,000	500,000,000
Current Services and Other Revenues	2,750,000,000	2,825,000,000	75,000,000
Tuition and Student Fees	745,000,000	745,000,000	-
Bonds	90,500,000	495,000,000	404,500,000
Tobacco Funds	153,200,000	147,800,000	(5,400,000)
Local Government Funds	49,800,000	49,800,000	-
Federal Essential Services Funds	139,632,600	-	(139,632,600)
Adjustment for Interfund Transfers	53,500,000	-	(53,500,000)
Reserve Transfers	(322,564,400)	352,890,400	675,454,800
Reversions - Underexpenditures	104,600,000	104,600,000	-
Rainy Day Fund Transfer	(39,000,000)	(58,400,000)	(19,400,000)
Total	\$ 22,270,000,000	\$ 24,100,000,000	\$ 1,830,000,000

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Program	Estimated Budget FY 2003-2004	Preliminary Budget FY 2004-2005	Difference
General Government	\$ 654,736,000	\$ 938,436,000	\$ 283,700,000
Education	6,020,009,000	6,253,943,000	233,934,000
Health and Social Services	10,828,350,000	11,539,597,000	711,247,000
Law, Safety, and Correction	1,157,161,000	1,172,004,000	14,843,000
Resources and Regulation	687,864,000	673,854,000	(14,010,000)
Business and Economic Development	434,087,000	452,051,000	17,964,000
Total General Fund	19,782,207,000	21,029,885,000	1,247,678,000
Transportation	1,443,590,000	1,619,845,000	176,255,000
Debt Service Requirements	228,163,000	250,800,000	22,637,000
Capital Outlay Program	70,232,000	397,930,000	327,698,000
Facilities Revolving Fund	99,608,000	136,240,000	36,632,000
Cities and Counties - State Shared Taxes	646,200,000	665,300,000	19,100,000
Total State Budget All Programs	\$ 22,270,000,000	\$ 24,100,000,000	\$ 1,830,000,000

Investment Policy

The Funding Board is charged with the establishment of the investment policy for the State. The State Treasurer is responsible for the management of the State Pooled Investment Fund (which includes the State's cash, various dedicated reserves and trust funds of the State, and the Local Government Investment Pool). The primary investment objective for the State Pooled Investment Fund is safety of principal, followed by liquidity and yield. No investments may be purchased with a remaining maturity of greater than 397 calendar days however, the weighted average maturity cannot exceed 90 days. Funds may be invested in collateralized certificates of deposit with authorized Tennessee financial institutions; bills, notes, and bonds of the U.S. Treasury; other obligations guaranteed as to principal and interest by the United States or any of its agencies; and repurchase agreements against obligations of the United States or its agencies. Securities underlying repurchase agreements must be direct obligations of the United States Government or other obligations guaranteed as to principal and interest by the United States or any of its agencies and held by the Federal Reserve Bank in the account of the State Trust of Tennessee or by a trustee-custodian under a tri-party contract between the Treasury Department, the broker-dealer, and the custodian bank. Funds may also be invested in prime commercial paper, prime banker's acceptances, certain securities lending agreements, and certain obligations of the State, pursuant to Section 9-4-602 (b), Tennessee Code Annotated. The State Trust of Tennessee, a non-profit corporation established in 1979, is a limited member of the Federal Reserve Bank System. (See Note 5 A. "Deposits and investments" to the financial statements of the State; see Appendix A.)

GASB 34

The Governmental Accounting Standards Board recently imposed significant new accounting standards on state and local governments pursuant to Statement No. 34 ("GASB 34"). GASB 34 is effective in fiscal year 2001-02 for state and local governments with over \$100 million or more in revenues. GASB 34 imposes several new requirements with respect to the financial statements prepared by state and local governments, including: (i) a requirement of detailed financial statements for any major fund (defined as a fund whose revenues, expenses, assets or liabilities are at least 10% of the corresponding totals for all government or enterprise funds and at least 5% of the aggregate amount for all government and enterprise funds); (ii) a budget analysis with a comparison to the original budget (as opposed to including only a comparison with the budget that has been revised throughout the course of the year); (iii) a required reporting of all capital assets, including infrastructure such as roads and bridges; and (iv) preparation of a management discussion and analysis letter (the "MD&A") for the purpose of providing an analytic overview of the government's financial activities, including an analysis of any significant changes in capital assets or long-term debt. The State implemented GASB 34 for the first time for the fiscal year ending June 30, 2002. The modified approach for infrastructure assets is used by the State. This means that infrastructure assets, and additions and improvements which increase the capacity or efficiency of these assets, will be capitalized but not depreciated, and expenditures made to preserve their useful life will be expensed and not depreciated.

Financial Reporting and Budgeting Awards

The Government Finance Officers Association of the United States and Canada (the "GFOA") has awarded Certificates of Achievement for Excellence in Financial Reporting both to the State of Tennessee for its comprehensive annual financial report every year since the fiscal year ended June 30, 1979 and to the Tennessee Consolidated Retirement System for its financial report every year since the fiscal year ended June 30, 1988. In order to be awarded a Certificate of Achievement for Excellence, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report, the content of which conforms to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

The GFOA also presented its Distinguished Budget Presentation Award to the State for its annual budget for the fiscal years ended June 30, 1992 through June 30, 1995 and June 30, 1998 through June 30, 2004. In order to receive this award, a governmental unit must publish a budget document that meets program criteria as a policy document, as an operations guide, as a financial plan and as a communication device.

DEBT OF CERTAIN AGENCIES AND AUTHORITIES

The following entities are the corporate governmental agencies and instrumentalities of the State authorized to issue various debt instruments. The State is not liable on any debt instrument issued by any of the following entities, and no such debt instrument is a debt or obligation of the State and the full faith and credit of the State is not pledged to the payment thereof.

The Tennessee Local Development Authority

In 1978, the General Assembly created the Tennessee Local Development Authority (the "TLDA") [Sections 4-31-101 et seq., Tennessee Code Annotated]. TLDA is authorized to loan funds to local governments for sewage treatment, waterworks, capital projects, fire fighting equipment, and airport facilities; and is authorized to loan funds to certain small business concerns for pollution control equipment. TLDA also is authorized to make funds available for loans for agricultural enterprises. TLDA is authorized to make loans to not-for-profit organizations providing certain mental health, mental retardation, and alcohol and drug services. TLDA is a corporate governmental agency and instrumentality of the State. In order to fund these loans, TLDA is empowered to issue bonds and notes in aggregate amounts outstanding not to exceed the following: \$302,805,000 for sewage treatment and waterworks facilities; \$10,000,000 for firefighting equipment; \$200,000,000 for airport facilities; \$50,000,000 for pollution control equipment; \$50,000,000 for capital projects; \$50,000,000 for mental health, mental retardation, and alcohol and drug services; and \$30,000,000 for agricultural enterprises.

Bonds and notes issued by TLDA are secured by: (i) in the case of loans to local governments, monies received by TLDA under loan program agreements with the local governments and by the local government's allocation of state-shared

taxes; (ii) in the case of loans to small business concerns, the monies received under agreements with those concerns; (iii) in the case of loans to not-for-profit organizations, monies received under State grant agreements and a pledge of the department of mental health and mental retardation's annual budget; and (iv) in the case of agricultural loans, the monies received under agreements with lenders and a pledge of any money, income or revenue from any source.

As of May 31, 2004, TLDA had \$34,465,000 (unaudited) of bonds and \$48,500,000 (unaudited) of bond anticipation notes outstanding for the making of loans for sewage treatment and waterworks facilities.

The Tennessee State School Bond Authority

In 1965, the General Assembly created the Tennessee State School Bond Authority (the "Authority") [Sections 49-3-1201 et seq., Tennessee Code Annotated]. The Authority is a corporate governmental agency and instrumentality of the State of Tennessee. The Authority is authorized to issue its bonds and notes to finance capital outlay programs for higher educational facilities which may be required or convenient for the purposes of The University of Tennessee, including its branches and divisions, and for the purposes of the institutions of higher education under the supervision and administration of the Tennessee Board of Regents of the State University and Community College System of the State of Tennessee. In 1980, the General Assembly further authorized the Authority to issue its bonds or notes to provide funds for the making of student loans by the Tennessee Student Assistance Corporation; however, no such bonds or notes have been issued for this purpose. The Authority also is authorized to issue Qualified Zone Academy Bonds ("QZAB") to finance improvement loans to cities and counties for qualifying K-12 schools.

Generally, all outstanding higher educational facility debt obligations of the Authority are secured by financing charges payable under contracts and agreements entered into by the Authority and the Board of Trustees of The University of Tennessee and the Tennessee Board of Regents of the State University and Community College System of the State of Tennessee, as successor to the State Board of Education; legislative appropriations; and certain funds and accounts established by the Higher Educational Facilities General Bond Resolutions of the Authority. The QZAB bonds are part of a Federal government program in which a Federal income tax credit is given to investors in lieu of interest on the bonds and are secured by the general obligation pledge of the borrowers and the unobligated state-shared taxes of the borrowers.

As of May 31, 2004, the Authority had outstanding \$504,147,024 (unaudited) aggregate principal amount of higher educational facility bonds (including accretion of College Savings Bonds), had outstanding \$27,156,000 (unaudited) of higher educational facility commercial paper, and had outstanding \$27,065,000 (unaudited) aggregate principal amount of QZAB bonds.

The Tennessee Housing Development Agency

In 1973, the General Assembly created the Tennessee Housing Development Agency (the "Agency"), [Sections 13-23-101 et seq., Tennessee Code Annotated (the "Tennessee Housing Development Agency Act")]. The Agency is authorized, among other things, to issue its bonds and notes to make funds available for the financing of decent, safe and sanitary residential housing for persons and families of lower and moderate income and to assist in coordinating Federal, state, regional and local public and private efforts and resources to increase the supply of residential housing.

The Agency has established a mortgage finance program and is making funds available for loans for residential housing for persons or families of lower and moderate income. Such loans are secured by eligible mortgages on the properties. The Agency has made, but does not currently make, loans for multi-family residential housing for rental occupancy.

In order to accomplish its objectives, the General Assembly has authorized the Agency to issue its bonds and notes, provided that the aggregate principal amount outstanding on such bonds and notes may not exceed \$2,050,000,000, excluding bonds and notes which have been refunded. The Agency's net indebtedness, excluding the refunded bonds, at May 31, 2004, was \$1,767,832,239.

Obligations of the Agency are secured by, among other things, mortgage loans made by the Agency from the proceeds of such obligations. The Tennessee Housing Development Agency Act provides a mechanism for certifying to the Governor and to the Commissioner of Finance and Administration amounts, if any, needed for debt service or operating expenses of the Agency and authorizes the General Assembly to appropriate, to expend and to provide for the payment of

such amounts, but imposes no legal obligation upon the General Assembly to do so. These provisions of the Tennessee Housing Development Agency Act do not constitute a legally enforceable obligation of the State to pay any such amounts. Under the Constitution of the State, no monies may be withdrawn from the Treasury but in consequence of appropriations made by law.

Watkins Institute

Watkins Institute (the "Institute") is an educational institution located in Nashville. Since 1881, the State has served as trustee of a trust providing for the maintenance of the Institute. On behalf of the State as trustee and with the approval of the State Senate, the Governor of the State appoints commissioners of the Institute, all as provided in the wills and codicils establishing the trust. In 1956, the Chancery Court of Davidson County determined that the Institute was a State agency for the purpose of providing capital improvements through the issuance of bonds. No such bonds have been issued.

State Veterans' Homes Board

In 1988, the General Assembly created the Tennessee State Veterans' Homes Board (the "Veterans' Homes Board") [Sections 58-7-101 to 58-7-112, inclusive, Tennessee Code Annotated]. A political subdivision and instrumentality of the State, the Veterans' Home Board is authorized to issue its debt instruments to finance public homes for the support and care of honorably discharged veterans of the United States armed forces. Such homes will be established only if Federal Veterans' Administration funds are available to provide a share of the construction and operation costs. Prior to the issuance of any debt instruments, the Veterans' Homes Board must receive the approval of the Funding Board.

All outstanding bonds of the Veterans' Homes Board were refunded and defeased by the State of Tennessee with the General Obligation Bonds, 2003 Series A.

THE TENNESSEE CONSOLIDATED RETIREMENT SYSTEM

The Tennessee Consolidated Retirement System ("TCRS") was established in 1972 to administer a retirement program for the public employees of the State. In 1972, the seven existing State retirement systems were closed, and all assets and liabilities of these superseded systems were transferred to the TCRS. TCRS provides retirement, disability and death benefits to TCRS members and their beneficiaries. These benefits are available to members at various times depending on their ages and creditable service records. Benefits are determined by a formula using the highest five-year average salary and years of service of each employee. Benefits are funded from contributions of members and employers. Contributions are determined on an actuarial reserve basis and provide funding for both normal and accrued liability costs. Effective July, 1981, pursuant to noncontributory legislation, contributions of up to five percent (5%) of the earnable compensation of most classes of general employees, formerly paid by those employees, were assumed by the State.

Through June 30, 2003, employers contributed \$398.3 million to TCRS while contributory members contributed \$197.7 million. The earnings on investments equaled a \$1.1 billion gain for the System through June 30, 2003. As a result of the positive cash flow for the TCRS, the reserves increased to \$23.8 billion as of June 30, 2003. The investment objective for TCRS is to obtain the highest available return on investments consistent with the preservation of principal while maintaining sufficient liquidity to react to the changing environment and to pay beneficiaries in a timely manner. TCRS emphasizes a conservative, high quality portfolio to ensure the soundness of TCRS and the ability to provide the needed funds upon a member's retirement. Funds in TCRS are actively managed with a diversified portfolio of high quality domestic and international stocks and bonds, mortgages and money market instruments. The investment policy of TCRS is established by the Board of Trustees of TCRS and may be more restrictive than the statutory authority.

An experience study of TCRS is conducted every four years. A new experience study was conducted as of June 30, 2000. The results of the 2001 actuarial valuation became effective on July 1, 2002. The investment assumption remains at 7 1/2% while the annual salary growth rate was reduced to approximately 4 3/4% as a result of a revised age graded salary scale.

In addition, an actuarial valuation is made every two years. The actuarial valuation as of July 1, 2001, incorporated the 2000 assumptions. For actuarial purposes, investments were valued using a five-year moving market average. With the 2001 actuarial valuation the accrued liability was reestablished. This was accomplished by setting the unfunded accrued

liability equal to the excess of the Entry Age Normal Past Service Liability over the valuation assets. An actuarial valuation was performed on July 1, 2003 and the results will be incorporated into contribution rates effective July 1, 2004.

The accrued liability of TCRS, based on the present value of benefits for past and future service, was estimated to be \$414.1 million at June 30, 2003. Of this accrued liability, \$74.0 million is attributable to the State of Tennessee. As of June 30, 2002, TCRS had 197,971 active members and 80,426 retired members; as of June 30, 2003, TCRS had 198,917 active members and 83,121 retired members.

The Governmental Accounting Standard Board "GASB" issued Statement No. 25 "*Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*", requiring information in the notes to the financial statements relating to the funding progress of a pension plan. Expressing the unfunded actuarial accrued liability as a percentage of annual covered payroll approximately adjusts for the effect of inflation and aids analysis of the progress made in accumulating sufficient assets to pay benefits when due. Generally, the smaller this percentage, the stronger the system. The fiscal year ended June 30, 2003 is presented in accordance with GASB Statement No. 25 as follows:

SETHEEPP/PSPP (Unaudited)

Schedules of Funding Progress
(Dollars Expressed in Thousands)

	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Frozen Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a-b)	Annual Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b-a)/c
SETHEEP	07/01/01	\$20,760,989	\$20,842,216	\$81,227	99.61%	\$4,451,452	1.82%
	07/01/99	18,327,133	18,420,156	93,023	99.49%	4,132,409	2.25%
	06/30/97	15,671,678	15,782,850	111,172	99.30%	3,810,231	2.92%
PSPP	07/01/01	3,187,990	3,528,137	340,147	90.36%	1,545,593	22.01%
	07/01/99	2,690,781	2,890,942	200,161	93.08%	1,341,363	14.92%
	06/30/97	2,226,891	2,287,904	61,013	97.33%	1,130,585	5.40%

The SETHEEP (State Employees, Teachers and Higher Education Employees Pension Plan) is comprised of a number of employee groups. However, the unfunded liability of \$81.2 million at July 1, 2001 is attributable to two employee groups: 1) County Officials employed prior to July 1, 1972 and 2) State Judges and Attorney General employed prior to July 1, 1972. The PSPP (Political Subdivision Pension Plan) represents 404 participating entities at July 1, 2001. The unfunded liability of \$340.1 million is attributable to 318 of the 404 entities.

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The information presented in the required supplementary Schedule of Funding Progress was determined as part of the latest actuarial valuations as of July 1, 2001. Additional information follows:

	SETHEPP (Unaudited)	PSSP (Unaudited)
Valuation Date	7/1/2001	7/1/2001
Actuarial cost method	Frozen Entry Age	Frozen Entry Age
Amortization method	Level Dollar	Level Dollar
Remaining amortization period	14 Years closed period	(1) closed period
Asset valuation method	5-year Moving Market Average	5-year Moving Market Average
Actuarial assumptions:		
Investment rate of return	7.50%	7.50%
Projected salary increases	4.75%(3)	4.75%(3)
Includes inflation at	(2)	(2)
Cost-of-living adjustments	3.00%	3.00%
Increase in Social Security wage base	3.50%	3.50%

(1) The length of the amortization period varies by political subdivision. For political subdivisions entering the plan on or after July 1, 1994, the amortization period does not exceed 20 years

(2) No explicit assumption is made regarding the portion attributable to the effect of inflation on salaries

(3) Uniform rate that approximates the effect of a graded salary scale.

LITIGATION

Due to its size and broad range of activities, the State and its officers and employees are involved in a number of legal actions. In view of the financial condition of the State, except with respect to *Tennessee Small Schools System v. Tennessee Commissioner of Education* and the disputed Federal financial participation in TennCare discussed below, it is the opinion of the Commissioner of Finance and Administration that the State's financial condition will not be materially affected by such litigation, based on information known at the date of this Official Statement.

In *Tennessee Small Schools System v. Tennessee Commissioner of Education et al.* (Davidson Chancery Court, Docket No. 88-1812-II), plaintiffs asserted that the State has not complied with a 1994 Tennessee Supreme Court decision that required the State to "equalize" teachers' salaries according to a certain formula. In October 2002, the Supreme Court ruled in favor of the plaintiffs and held that the State's teacher salary equity plan failed to comply with the State's constitutional obligation to formulate and maintain a system of public education that afforded substantially equal educational opportunity to all Tennessee K-12 students. The State has complied with the order by appropriating money in the 2003 and 2004 legislative sessions to teacher pay equalization. To the extent that additional funds are needed to comply with the Supreme Court's 2002 order, the funds will be appropriated in the regular budget process.

On January 1, 1994, after receiving a waiver from the United States Department of Health and Human Services, the State replaced a substantial portion of its Medicaid Program with a managed care demonstration project called TennCare. TennCare is the subject of litigation.

The following four TennCare related class actions are all encompassed in a global settlement, the terms of which have been approved by the Governor, Comptroller, Attorney General, and Speakers and presented to and approved by the respective courts in which the cases are pending. The terms of the global settlement are set out following this listing of the individual cases. *Grier, et al. v. Goetz, et al.* (U.S. District Court, M. D. Tenn.) deals with the procedural protections to be

afforded all enrollees when TennCare services are denied, delayed, suspended, or terminated. A revised consent decree, entered on October 26, 1999 and modified by order entered September 25, 2003, sets out due process requirements. *Rosen, et al. v. Commissioner of Finance and Administration* (U.S. District Court, M. D. Tenn.), a class action filed on behalf of all waiver eligible TennCare enrollees, deals with the due process protections to be afforded to persons whose TennCare applications are denied or whose TennCare coverage is terminated. An order entered in December 2002 ordered the reinstatement of all of the approximately 200,000 enrollees who had been terminated during the redetermination process that began July 1, 2002, and effectively precluded implementation of the new TennCare waiver. The State appealed to the Court of Appeals for the Sixth Circuit, which granted a stay of that order pending appeal. *John B., et al. v. Goetz, et al.* (U.S. District Court, M. D. Tenn.) is a class action brought on behalf of all TennCare enrollees under the age of 21, alleging that the State was not meeting its obligation to provide these children with the early and periodic screening, diagnosis, and treatment (EPSDT) services required by the federal Medicaid Act. The case was settled by a consent decree in March 1998. In an opinion filed in December 2001, following a hearing on plaintiffs' motion for a finding of contempt, the court found that the State was in violation of federal EPSDT law. A special master was appointed by the court to assist it in monitoring the State's compliance. In a recent development not affected by the global settlement, plaintiffs have filed a motion for a hearing on the current status of the State's compliance with the consent decree. *Newberry, et al. v. Goetz, et al.* (U.S. District Court, M. D. Tenn.) is a class action filed as a challenge to TennCare policies and practices related to the provision of home health services to enrollees. The complaint was later expanded to challenge a proposed limit of 125 health visits a year.

The terms of the global settlement with respect to each of the above cases are as follows: In *Grier*, the principal feature of the agreement is a time-limited modification of the pharmacy provisions of the revised consent decree, shortening from two weeks to three days the minimum amount of prescribed medications that must be dispensed to an enrollee on an interim basis. In *Rosen*, the State has agreed to extend a grace period for reapplication to all former TennCare enrollees who lost their coverage as a result of the redetermination process that began July 1, 2002. The benefit reductions and cost sharing increases that were to have gone in effect under the new TennCare waiver have been withdrawn. In an order entered October 15, 2003, the District Court set aside its order of December 18, 2002. In *John B.*, the benefits reductions that were to have taken effect under the new waiver and which have now been withdrawn included the elimination of EPSDT coverage for non-Medicaid eligible children. The District Court was notified of the withdrawal of the proposed benefits reduction. In *Newberry*, the State must ensure that TennCare enrollees receive home health care from the MCOs as medically necessary. The settlement also provides for the withdrawal of the proposed reduction of home health care benefits and the proposed elimination of private duty nursing benefits. The financial impact on the State of these changes will depend on the at-risk status of the MCOs and the level of utilization of these services. A further aspect of the settlement agreement, although it is not a term that is judicially enforceable, is the State's commitment to work to develop home and community-based alternatives to nursing home placement. An express condition of that agreement is that it must be budget neutral to the State.

In *Universal Care of Tennessee, Inc. v. M.D. Goetz and Manny Martins, in their Official Capacities*, (Tennessee Claims Commission No. 20301822), Universal Care, a former managed health care company, claims the State did not act in good faith and breached its TennCare contract by failing to pay actuarially sound rates sufficient to cover the health care costs of the TennCare enrollees served by Universal. The company, which is now insolvent and in receivership, is seeking approximately \$100 million in damages in a claim that the State will vigorously defend.

Brown v. Tenn. Dept. of Finance and Administration (U.S. District Court, Middle District of Tennessee, No. 3-00-0665) is a class action filed on behalf of individuals with mental retardation and other developmental disabilities waiting for services to which they are entitled under the Medicaid program. The State currently has at least 2,900 persons on a waiting list for these services. The plaintiffs assert that the statutory limit on the number of ICF/MR beds and the restriction on the number of individuals able to be served under the Home and Community-Based Services Waiver violate the right of eligible Tennesseans to receive services in an adequate amount, duration and scope and with reasonable promptness as required by the Medicaid Act. The State is engaged in settlement negotiations with the plaintiffs.

United State of America v. State of Tennessee (Arlington Developmental Center) (U.S. District Court, W.D.) is a case brought pursuant to the Civil Rights of Institutionalized Persons Act, alleging that the constitutional rights of residents at Arlington were being violated. The trial was in August, 1993. A remedial order was approved on September 1, 1994. Since entry of the remedial order, six separate contempt actions have been filed. Some of these have resulted in fines against the State. The court subsequent to the remedial order has issued an order interpreting the third category of the definition of class, i.e., persons at risk of being placed at Arlington Developmental Center, to consist of all individuals who reside in West Tennessee and who have demonstrated medical needs sufficient to require institutional care in the absence of home or community-based services. This interpretation increases the number of class members from 452 to an estimated 3,000. A

notice of appeal was filed with the 6th Circuit Court of Appeals and a stay granted. An agreement to resolve this issue was not approved by the District Court.

On December 19, 1994, the Health Care Financing Administration, currently the Centers for Medicare and Medicaid Services (“CMS”), notified the State that the State’s inclusion of amounts received from its nursing home bed tax and services tax in computing the amount of Federal financial participation was under review and was possibly inconsistent with Federal methodology for such computation due to an alleged impermissible “hold harmless” State grant arrangement. On January 19, 2001, the State received notice of disallowance relating to the nursing home bed tax of Federal funds in the amount of \$519,864,853 for the period October 1992 through September 2000. On June 11, 2001, the State received a second notice of disallowance relating to the nursing home bed tax in the amount of \$32,744,000 for the period October 2000 through March 2001. The State is appealing administratively CMS’s assertion of improper computation of the amount of Federal financial participation. If it were ultimately determined that the State’s inclusion of these taxes was inconsistent with Federal methodology for such computation, then CMS would offset the disallowed amounts against future Federal participation in TennCare. The State eliminated the State grant arrangement as of August 1, 2001, and does not believe that its inclusion of these taxes after that date will be challenged by CMS.

At this time there is one lawsuit pending against the State of Tennessee that could affect the tobacco settlement payments. The original complaint was dismissed but the plaintiffs are appealing. In addition, the Independent Auditor responsible for disbursing settlement payments may elect to preliminarily make adjustments to the State’s tobacco settlement payments without resorting to litigation. These potential adjustments, most notably relating to volume and non-participating manufacturers, have been made in the past and may be made in the future. Also, tobacco companies could unilaterally withhold payments owed to the State. The State may vigorously dispute any such adjustments or withholdings, but it could take years to have those disputes resolved. Lastly, litigation in other states may have a material effect on the tobacco settlement payments to the State.

TAX MATTERS

Federal Tax Matters

General

The following is a brief discussion of certain Federal income tax consequences to U.S. Holders (as defined herein) of the purchase, ownership and disposition of the Bonds under existing law. This discussion is based on certain relevant provisions of the Code under existing law and does not purport to address all aspects of Federal taxation that affect particular investors in light of their individual circumstances. This discussion is limited to investors who hold the Bonds as “capital assets” under Section 1221 of the Code, which generally mean property held for investment. Prospective investors, particularly those who may be subject to special rules, should consult their own tax advisors regarding the Federal tax consequences of owning and disposing of the Bonds.

U.S. Holder

The discussion of Federal income tax consequences herein only relates to U.S. Holders of the Bonds. As used herein, the term “U.S. Holder” means a beneficial owner of a Bond that is for Federal income tax purposes one of the following: (i) a citizen or resident of the United States; (ii) a corporation, partnership, or other entity created or organized in or under the laws of the United States or any State or the District of Columbia; (iii) an estate the income of which is subject to United States Federal income taxation regardless of its source; or (iv) a trust whose administration is subject to the primary jurisdiction of a United States court and which has one or more United States persons who have the authority to control substantial decisions of the trust.

Interest Income Taxable

In general, interest on the Bonds, including prescribed “qualified stated interest” that is payable at least annually at prescribed rates and accrued original issue discount, is included in the gross income of the owners as ordinary interest income for Federal income tax purposes. Except for original issue discount, which accrues under special rules discussed below,

interest income on the Bonds is included in the gross income of the owners when accrued or received in accordance with an owner's regular method of Federal tax accounting.

Sale, Exchange, or Other Disposition

In general, upon the sale, exchange, or redemption of a Bond, an owner will recognize taxable gain or loss in an amount equal to the difference between the amount realized (excluding any accrued qualified stated interest which will be taxable as such) and the owner's adjusted tax basis in the Bond. An owner's adjusted tax basis in a Bond generally will equal the owner's initial cost of the Bond, plus accrued OID and accrued market discount previously included in the owner's taxable income, less any bond premium previously amortized, and less any payments previously received on the Bond besides qualified stated interest. Such gain or loss generally will be capital gain or loss. Such gain or loss generally will be long-term capital gain or loss if the owner has held the Bond for more than one year. Subject to various special rules, the Code provides preferential treatment for certain net long-term capital gains realized by individuals and generally limits the use by any taxpayer of capital losses to reduce ordinary income.

Defeasance

Owners of the Bonds should be aware that, for Federal income tax purposes, the deposit of moneys or securities in such amount and manner as to cause the Bonds to be deemed to be no longer outstanding under the Bond Resolution (a "defeasance") could result in a deemed exchange under Section 1001 of the Code and a recognition by such owner of taxable income or loss, without any corresponding receipt of moneys. In addition, for Federal income tax purposes, the character and timing of receipt of payments on the Bonds subsequent to any such defeasance could also be affected. Owners of the Bonds should consult with their own tax advisors regarding the consequences of a defeasance for Federal income tax purposes, and for State and local tax purposes.

Backup Withholding and Information Reporting

In general, information reporting requirements will apply to non-corporate owners of the Bonds with respect to payments of the principal of and interest on the Bonds and proceeds of sale of such Bonds before maturity within the United States. Backup withholding, at various rates according to the year, will apply to such payments unless the owner: (i) is a corporation or other exempt recipient and, when required, demonstrates that fact; or (ii) provides a correct taxpayer identification number, certifies under penalties of perjury when required that such owner is not subject to backup withholding, and has not been notified by the Internal Revenue Service that it has failed to report all interest and dividends required to be shown on its United States Federal income tax returns.

State of Tennessee Tax Matters

In the opinion of Bond Counsel to the State, under existing laws of the State, the Bonds and the interest thereon are free from taxation by the State or any county, municipality or taxing district of the State, except for inheritance, transfer and estate taxes and except to the extent such interest may be included within the measure of privilege taxes imposed pursuant to the laws of the State.

Bond Counsel expresses no opinion regarding any other state or local tax consequences with respect to the Bonds. Bond Counsel renders its opinion under existing statutes and court decisions as of the issue date and assumes no obligation to update its opinion after the issue date to reflect any future action, fact or circumstance, or change in law or interpretation or otherwise. Bond Counsel expresses no opinion as to the effect of any action hereafter taken or not taken, in reliance upon an opinion of other counsel, under state and local tax law.

For the proposed form of opinion of Bond Counsel relating to State tax matters, see Appendix C.

FINANCIAL ADVISOR

Public Financial Management, Inc. ("PFM") is employed by the State to perform professional services in the capacity of financial advisor. In its role as financial advisor to the Funding Board, PFM has provided advice on the plan of financing and structure of the Bonds, reviewed certain legal and disclosure documents, including this Official Statement, for financial matters, and reviewed and gave an opinion on the fairness of the pricing of the bonds by the underwriting syndicate. PFM

has not independently verified the factual information contained in this Official Statement, but relied on the information supplied by the State and other sources and the State's certification as to the Official Statement.

VERIFICATION AGENT

The accuracy of the arithmetical computations of the adequacy of the cash and maturing principal and interest earned on the Government Obligations deposited in the Refunding Trust Fund to pay, when due, the principal of, premium if any, and interest on the Refunded Bonds was verified by McGladrey & Pullen LLP, a firm of independent certified public accountants.

UNDERWRITING

UBS Financial Services Inc., as representative and on behalf of the Underwriters, has agreed to purchase and to pay a net purchase price for the Series A Bonds of \$11,844,871.11 (representing an aggregate principal amount of \$11,885,000.00 less Underwriters' discount of \$40,128.89), plus accrued interest to the delivery date, and for the Series B Bonds a net purchase price of \$42,795,657.75 (representing an aggregate principal amount of \$42,950,000.00 less Underwriters' discount of \$154,342.25), plus accrued interest to the delivery date.

The prices and other terms respecting the offering and sale of the Bonds may be changed from time to time by the Underwriters after such Bonds are released for sale, and the Bonds may be offered and sold at prices other than the initial offering prices, including sales to dealers who may sell the Bonds into investment accounts.

RATINGS

Fitch Ratings, Moody's Investors Service, Inc., and Standard & Poor's Ratings Services have given the Bonds ratings of AA, Aa2, and AA, respectively. Such ratings reflect only the respective views of such organizations and an explanation of the significance of a rating may be obtained only from the rating agency furnishing the same. There is no assurance that any rating will be maintained for a given period of time or that it will not be revised downward or withdrawn entirely by the rating agency if in its judgment, circumstances so warrant. Any such downward revision or withdrawal of ratings may have an adverse affect on the market price of the Bonds.

APPROVING LEGAL OPINIONS

The validity of the Bonds will be approved by the legal opinion of Hawkins Delafield & Wood LLP, New York, New York, Bond Counsel to the State. For the proposed form of Bond Counsel opinion relating to the Bonds, see Appendix C. Certain legal matters will be passed upon by the Attorney General and Reporter of the State of Tennessee, as counsel to the Funding Board. Certain legal matters will be passed upon for the Underwriters by their counsel, Bass, Berry & Sims, PLC, Nashville, Tennessee. No representation is made to the holders of the Bonds that any of such counsel have verified the accuracy, completeness or fairness of the statements in this Official Statement, and such counsel assume no responsibility to the holders of the Bonds except for the matters that will be set forth in their respective opinions.

CONTINUING DISCLOSURE

The State has authorized a Continuing Disclosure Undertaking (the "Undertaking") with respect to the Bonds to assist the Underwriters in complying with U.S. Securities and Exchange Commission Rule 15c2-12(b)(5). The Undertaking will be for the benefit of the holders of the Bonds, and beneficial owners will be third-party beneficiaries thereof. The form of the undertaking is included herein as Appendix E.

The State has not failed to comply in any material respect with any previous undertaking in a written contract or agreement specified in the Rule.

MISCELLANEOUS

Any statements in this Official Statement involving matters of opinion or estimates, whether or not expressly so stated, are intended as such and not as representatives of fact. No representation is made that such statements will be realized.

All financial and other information presented in this Official Statement has been provided by the State from its records, except for information expressly attributed to other sources. The presentation of information, including tables of receipts from taxes and other revenues, is intended to show recent historic information, and it is not intended to indicate future or continuing trends in the financial position or other affairs of the State. No representation is made that past experience, as it might be shown by such financial and other information, will necessarily continue or be repeated in the future.

References to and summaries of provisions of the Constitution and laws of the State or of any other documents referred to in this Official Statement are qualified in their entirety by reference to the complete provisions thereof.

This Official Statement is not to be construed as a contract or agreement between the State and the purchasers or holders of any of the Bonds.

STATE OF TENNESSEE

By: /s/ John G. Morgan
Comptroller of the Treasury;
Secretary of the Funding
Board of the State of
Tennessee

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Financial Statements

The Comprehensive Annual Financial Report (“CAFR”) of the State, including the audited General Purpose Financial Statements, for the fiscal year ended June 30, 2003 has been filed with each nationally recognized municipal securities information repository (“NRMSIR”)(see “Continuing Disclosure”) and is obtainable from them in accordance with their respective procedures. A printed version is also available upon request to the Funding Board, James K. Polk State Office Building, Suite 1600, 505 Deaderick Street, Nashville, Tennessee 37243-0273, telephone (615) 401-7872, fax (615) 741-5986. The CAFR has been posted on the State’s website at www.state.tn.us/finance/act/cafr.html.

The following reports, each of which are included in the CAFR and have been posted on the State’s website, are incorporated herein by reference:

Auditor’s Report

Management’s Discussion and Analysis

Government-wide Financial Statements:

Statement of Net Assets

Statement of Activities

Fund Financial Statements:

Balance Sheet-Governmental Funds

Statement of Revenues, Expenditures, and Changes in Fund Balances-Governmental Funds

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balances of Governmental Funds to the Statement of Activities

Statement of Net Assets-Proprietary Funds

Statement of Revenues, Expenses, and Changes in Fund Net Assets-Proprietary Funds

Statement of Cash Flows-Proprietary Funds

Statement of Fiduciary Net Assets-Fiduciary Funds

Statement of Changes in Fiduciary Net Assets-Fiduciary Funds

Required Supplementary Information:

Schedule of Revenues, Expenditures, and Changes in Fund Balances-Budget and Actual-Major Governmental Funds

Reconciliation of Budget to GAAP-Note to RSI

Infrastructure Assets Reported Using the Modified Approach

Notes to the Financial Statements:

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Statistical and Economic Data

The Comprehensive Annual Financial Report (“CAFR”) of the State, including selected statistical data (unaudited), for the fiscal year ended June 30, 2003 has been filed with each nationally recognized municipal securities information repository (see “Annual Audits; Secondary Market Disclosures”) and is obtainable from them in accordance with their respective procedures. A printed version is also available upon request to the Funding Board, James K. Polk State Office Building, Suite 1600, 505 Deaderick Street, Nashville, Tennessee 37243-0273, telephone (615) 401-7872, fax (615) 741-5986. The CAFR has been posted on the State’s website at www.state.tn.us/finance/act/cafr.html.

The following statistical data, all of which is included in the CAFR and has been posted on the State’s website, is incorporated herein by reference:

Revenue by Source and Transfers In – All Governmental Fund Types

Expenditures by Function and Transfers Out – All Governmental Fund Types

Tax Revenues by Source – All Governmental Fund Types

Description of Tax Sources – All Governmental Fund Types

Ratio of Net General Long-Term Debt to Assessed Value and Net Debt Per Capita

Computation of Legal Debt Service Margin

Ratio of Annual Debt Service for General Long-Term Debt to Total Expenditures – All Governmental Fund Types

Schedule of Revenue Bond Coverage – Component Units – Tennessee Housing Development Agency and College and University Funds

Schedule of Fees/Charges, Legislative Appropriations and Debt Service

Economic Characteristics

Tennessee's Economic Growth

Manufacturing

Industrial Growth in Tennessee

Agriculture

Population and Employment Trend

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Form of Proposed Opinion of Bond Counsel

July 7, 2004

The Honorable Governor and Members of
the Funding Board of the State of Tennessee
Nashville, Tennessee 37243

Dear Sirs:

**STATE OF TENNESSEE
GENERAL OBLIGATION BONDS
2004 REFUNDING SERIES A (FEDERALLY TAXABLE), \$11,885,000
2004 REFUNDING SERIES B (FEDERALLY TAXABLE)), \$42,950,000**

At your request we have examined into the validity of \$11,885,000 General Obligation Bonds, 2004 Refunding Series A (Federally Taxable) (the "Series A Bonds") and \$42,950,000 General Obligation Bonds, 2004 Refunding Series B (Federally Taxable) (the "Series B Bonds" and, collectively with the Series A Bonds, the "Bonds") of the State of Tennessee (the "State"). The Bonds are dated as of June 1, 2004, and mature, are payable and bear interest, and the Series B Bonds are subject to redemption prior to maturity and to mandatory and optional tender for purchase, all as provided in the resolution of the Funding Board hereinafter mentioned.

The Bonds recite that they are issued under and pursuant to and in full compliance with the Constitution and laws of the State, including specifically Title 9, Chapter 9, Tennessee Code Annotated, various Public Acts of the General Assembly of the State of Tennessee, and a resolution adopted by the Funding Board of the State of Tennessee on May 27, 2004, to provide for the refunding of certain of the State's outstanding general obligation bonds.

We have examined the Constitution and statutes of the State; certified copies of proceedings of the Funding Board of the State of Tennessee and Public Acts of the General Assembly of the State of Tennessee authorizing the issuance of the Bonds, and an executed Bond, and have made such other examination of law and fact, as we have considered appropriate for purposes of this opinion.

Based on the foregoing, we are of the opinion that:

(1) The Bonds have been authorized and issued in accordance with the Constitution and laws of the State, and constitute valid general obligations of the State for the payment of which as to both principal and interest the full faith and credit of the State is pledged. As additional security for all of the Bonds and interest thereon there is also pledged the annual proceeds of a tax of up to five cents per gallon upon gasoline; the annual proceeds of a special tax of one cent per gallon on petroleum products; one-half of the annual proceeds of motor vehicle registration fees now or hereafter required to be paid to the State, and the annual proceeds of the franchise taxes imposed by the franchise tax law of the State. All of the Bonds, together with interest thereon, are entitled to the benefit of the foregoing taxes, fees, and revenues and to share therein pro rata with any other obligations of the State that might be entitled to share therein as provided by Sections 9-9-101 to 9-9-208, inclusive, Tennessee Code Annotated. The State has not waived immunity from suit or extended its consent to be sued. Monetary actions against the State for breach of contractual obligations may be heard and determined under current law exclusively in the Tennessee Claims Commission, an administrative tribunal, where the State may be liable only for actual damages and certain costs.

(2) Interest on the Bonds is includable in gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended.

(3) Under the existing laws of the State, the Bonds and the interest thereon are free from taxation by the State or any county, municipality or taxing district of the State, except for inheritance, transfer and estate taxes and except to the extent such interest may be included within the measure of privilege taxes imposed pursuant to the laws of the State.

The opinions expressed in paragraph (1) above are subject to applicable bankruptcy, insolvency, reorganization, moratorium and other laws heretofore or hereafter enacted affecting creditors' rights, and are subject to the application of principles of equity relating to or affecting the enforcement of contractual obligations, whether such enforceability is considered in a proceeding in equity or at law.

We express no opinion herein as to (i) Federal, state or local tax consequences arising with respect to the Bonds, or the ownership or disposition thereof, except as stated in paragraphs (2) and (3) above, (ii) the effect of any action taken or not taken, in reliance upon an opinion of other counsel, under state or local tax law, or (iii) the accuracy, adequacy, sufficiency or completeness of the Official Statement dated June 23, 2004 (or any update or amendment thereof or supplement thereto) relating to the Bonds, or any other financial or other information which has been or may be supplied to purchasers or prospective purchasers of the Bonds.

This opinion is issued as of the date hereof, and we assume no obligation to update, revise or supplement this opinion to reflect any future action, fact or circumstance, or change in law or interpretation or otherwise.

Very truly yours,

BOOK-ENTRY ONLY SYSTEM

The Depository Trust Company (“DTC”), New York, New York, will act as securities depository for the Bonds. The Bonds will be issued as fully-registered bonds registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Bond certificate will be issued for each maturity of each Series of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

Purchases of Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“Beneficial Owner”) is in turn to be recorded on the Direct and Indirect Participant’s records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

To facilitate subsequent transfers, all Bonds deposited by Direct Participants with DTC are registered in the name of DTC’s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Bonds; DTC’s records reflect only the identity of the Direct Participants to whose accounts such Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holding on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory and regulatory requirements as may be in effect from time to time. Beneficial Owners of Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. For example, Beneficial Owners of Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to Cede & Co. If less than all of the Bonds of a maturity within a Series are being redeemed, DTC’s practice is to determine by lot the amount of the interest of each Direct Participant in such maturity of such Series to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Bonds unless authorized by a Direct Participant in accordance with DTC’s procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the

State as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, interest and redemption premium, if any, payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the State or any Paying Agent, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC or the State or any Paying Agent, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, interest and redemption premium, if any, to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the State or any Paying Agent, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct or Indirect Participants.

A Beneficial Owner shall give notice to elect to have its Series B Bonds purchased or tendered, through its Participant, to the Tender Agent and the Remarketing Agent, and shall effect delivery of such Series B Bonds by causing the Direct Participant to transfer the Participant's interest in the Series B Bonds, on DTC's records, to the Tender Agent. The requirement for physical delivery of Series B Bonds in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the Series B Bonds are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered Series B Bonds to the Tender Agent for DTC's account.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the State. Under such circumstances, in the event that a successor securities depository is not obtained, Bond certificates are required to be prepared and delivered.

The State may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Bond certificates will be prepared and delivered to DTC.

THE FOREGOING INFORMATION CONCERNING DTC AND DTC'S BOOK-ENTRY ONLY SYSTEM HAS BEEN OBTAINED FROM DTC, A SOURCE THAT STATE BELIEVES TO BE RELIABLE, BUT THE STATE TAKES NO RESPONSIBILITY FOR THE ACCURACY THEREOF. NEITHER THE STATE, THE UNDERWRITERS, NOR THE PAYING AGENT AND REGISTRAR CAN MAKE ANY ASSURANCE THAT DTC OR THE DTC PARTICIPANTS WILL ACT IN A MANNER DESCRIBED HEREIN, NOR WILL THEY HAVE ANY RESPONSIBILITY OR OBLIGATION TO THE DTC PARTICIPANTS OR BENEFICIAL OWNERS FOR (1) SENDING TRANSACTION STATEMENTS; (2) MAINTAINING, SUPERVISING OR REVIEWING, OR THE ACCURACY OF, ANY RECORDS MAINTAINED BY DTC OR ANY DTC PARTICIPANT; (3) PAYMENT OR THE TIMELINESS OF PAYMENT BY DTC ANY DIRECT DTC PARTICIPANT, OR BY ANY DIRECT DTC PARTICIPANT OR INDIRECT DTC PARTICIPANT TO ANY BENEFICIAL OWNER OF ANY AMOUNT DUE TO ANY BENEFICIAL OWNER IN RESPECT TO THE PRINCIPAL OR REDEMPTION PREMIUM IF ANY, OR INTEREST ON BONDS; (4) DELIVERY OR TIMELY DELIVERY BY DTC OR ANY DTC PARTICIPANT TO ANY BENEFICIAL OWNER OF ANY NOTICE (INCLUDING NOTICE OF REDEMPTION) OR OTHER COMMUNICATIONS TO ANY BENEFICIAL OWNER WHICH IS REQUIRED OR PERMITTED UNDER THE TERMS OF THE BOND DOCUMENTS TO BE GIVEN TO BONDHOLDERS; (5) THE SELECTION OF THE BENEFICIAL OWNERS TO RECEIVE PAYMENT IN THE EVENT OF ANY PARTIAL REDEMPTION OF BONDS; OR (6) ANY ACTION TAKEN BY DTC OR ITS NOMINEE AS THE REGISTERED OWNER OF THE BONDS.

So long as Cede & Co. is the registered owners of the Bonds, as nominee for DTC, references in the Official Statement to the Bondholders or registered owners of the Bonds (other than under the caption "Tax Matters" in the Official Statement) shall mean Cede & Co. or any other DTC nominee, as aforesaid, and shall not mean the Beneficial Owners of the Bonds.

CONTINUING DISCLOSURE UNDERTAKING

This Continuing Disclosure Undertaking (the "Undertaking") is dated and made as of July 7, 2004, by the State of Tennessee (the "State") in connection with the issuance of the State's \$11,885,000 aggregate principal amount of General Obligation Bonds, 2004 Refunding Series A (Federally Taxable) and \$42,950,000 aggregate principal amount of General Obligation Bonds, 2004 Refunding Series B (Federally Taxable) (Variable Rate) (collectively, the "Bonds"). As authorized by Section 11 of the resolution (the "Bond Resolution") of the Funding Board of the State of Tennessee (the "Funding Board") adopted on May 27, 2004, authorizing the Bonds, the State agrees as follows:

ARTICLE I

Definitions

Section 1.1. Definitions. The following terms used in this Undertaking shall have the following respective meanings:

(1) "Annual Financial Information" means (i) updated versions of the following financial information and operating data contained in, or incorporated by reference pursuant to an Appendix to, the Official Statement with respect to the State, for each fiscal year of the State:

- Collections for Special Taxes
- Total Sales and Use Tax Collections
- Allocation of Sales and Use Tax to Debt Service
- General Obligation Bonds Outstanding
- Maximum and Actual Principal Amounts of Commercial Paper Outstanding
- Outstanding General Obligation Bonded Indebtedness, by Fiscal Year and Maturity
- Outstanding Debt of Certain Agencies and Authorities
 - Tennessee Local Development Authority
 - Tennessee State School Bond Authority
 - Tennessee Housing Development Agency
 - Watkins Institute
 - State Veterans' Homes Board
- Tennessee Consolidated Retirement System
 - Employers and Contributory Members Contributions
 - Reserves
 - Accrued Liability
 - Accrued Liability Attributable to State
 - Active/Inactive Members
 - Supplementary Information:
 - Schedules of Funding Progress (if required)
 - Unfunded Liability by groups (if required)
 - Supplementary Information (if required by use of frozen entry age actuarial method)
 - Additional Information relating to Required Supplementary Information
- The statistical data incorporated by reference in Appendix B to the Official Statement

and (ii) the information regarding amendments to this Undertaking required pursuant to Sections 4.2(c) and (d) of this Undertaking. Annual Financial Information shall include Audited Financial Statements, if available, or Unaudited Financial Statements.

The descriptions contained in clause (i) above of financial information and operating data constituting Annual Financial Information are of general categories or types of financial information and operating data. When such descriptions include information that no longer can be generated because the operations to which it related have been materially changed or discontinued, a statement to that effect shall be provided in lieu of such information.

(2) "Audited Financial Statements" means the annual financial statements of the State, audited by the Comptroller of the Treasury, Division of State Audit, as now required by State law (or such other auditor as hereafter may be required or permitted by State law). Audited Financial Statements shall be prepared in accordance with GAAP.

(3) "Counsel" means Hawkins Delafield & Wood LLP or other nationally recognized bond counsel or counsel expert in federal securities laws, in each case acceptable to the State.

(4) "GAAP" means generally accepted accounting principles for governmental units as prescribed by the Governmental Accounting Standards Board, the Financial Accounting Standards Board, or any successor to the duties and responsibilities of either of them.

(5) "Material Event" means any of the following events with respect to the Bonds, if material:

- (i) principal and interest payment delinquencies;
- (ii) non-payment related defaults;
- (iii) unscheduled draws on debt service reserves reflecting financial difficulties;
- (iv) unscheduled draws on credit enhancements reflecting financial difficulties;
- (v) substitution of credit or liquidity providers, or their failure to perform;
- (vi) adverse tax opinions or events affecting the tax-exempt status of the security;
- (vii) modifications to rights of security holders;
- (viii) bond calls;
- (ix) defeasances;
- (x) release, substitution, or sale of property securing repayment of the securities; and
- (xi) rating changes.

(6) "MSRB" means the Municipal Securities Rulemaking Board established pursuant to the provisions of Section 15B (b) (1) of the Securities Exchange Act of 1934.

(7) "NRMSIR" means, at any time, a then-existing nationally recognized municipal securities information repository, as recognized from time to time by the SEC for the purposes referred to in the Rule. NRMSIRs currently are identified on the SEC website at <http://www.sec.gov/consumer/nrmsir/htm>.

(8) "Official Statement" means the Official Statement dated June 23, 2004, of the State relating to the Bonds.

(9) "Rule" means Rule 15c2-12 promulgated by the SEC under the Securities Exchange Act of 1934 (17 CFR Part 240, §240.15c2-12), as in effect on the effective date hereof, including any official interpretations thereof.

(10) "SEC" means the United States Securities and Exchange Commission.

(11) "SID" means, at any time, a then-existing state information depository, if any, as operated or designated as such by or on behalf of the State for the purposes referred to in the Rule. As of the date hereof, there is no SID.

(12) "Unaudited Financial Statements" means the same as Audited Financial Statements, except that they shall not have been audited.

ARTICLE II

The Undertaking

Section 2.1. Purpose. This Undertaking is being executed, delivered and made solely to assist the underwriters of the Bonds in complying with subsection (b)(5) of the Rule.

Section 2.2. Annual Financial Information.

(a) The State shall provide Annual Financial Information with respect to each fiscal year of the State, commencing with the fiscal year ending June 30, 2004, by no later than 7 months after the end of the respective fiscal year, to each NRMSIR and the SID.

(b) The State shall provide, in a timely manner, notice of any failure of the State to provide the Annual Financial Information by the date specified in subsection (a) above to (i) either the MSRB or each NRMSIR, and (ii) the SID.

Section 2.3 Audited Financial Statements. If not provided as part of Annual Financial Information by the date required by Section 2.2(a) hereof because not available, the State shall provide Audited Financial Statements, when and if available, to each NRMSIR and the SID.

Section 2.4 Notices of Material Events.

(a) If a Material Event occurs, the State shall provide, in a timely manner, notice of such Material Event to (i) either the MSRB or each NRMSIR and (ii) the SID.

(b) Any such notice of a defeasance of Bonds shall state whether the Bonds have been escrowed to maturity or to an earlier redemption date and the timing of such maturity or redemption.

Section 2.5 Additional Disclosure Obligations. The State acknowledges and understands that other State and federal laws, including but not limited to the Securities Act of 1933 and Rule 10b-5 promulgated under the Securities Exchange Act of 1934, may apply to the State and that, under some circumstances, additional disclosures or other action in addition to those required by this Undertaking may be required to enable the State to fully discharge all of its duties and obligations under such laws.

Section 2.6. Additional Information. Nothing in this Undertaking shall be deemed to prevent the State from disseminating any other information, using the means of dissemination set forth in this Undertaking or any other means of communication, or including any other information in any Annual Financial Information or notice of a Material Event hereunder, in addition to that which is required by this Undertaking. If the State chooses to do so, the State shall have no obligation under this Undertaking to update such additional information or include it in any future Annual Financial Information or notice of a Material Event hereunder.

Section 2.7. No Previous Non-Compliance. The State represents that since July 3, 1995, it has not failed to comply in any material respect with any previous undertaking in a written contract or agreement specified in paragraph (b)(5)(i) of the Rule.

ARTICLE III

Operating Rules

Section 3.1. Reference to Other Documents. It shall be sufficient for purposes of Section 2.2 hereof if the State provides Annual Financial Information by specific reference to documents (i) either (1) provided to each NRMSIR existing at the time of such reference and the SID or (2) filed with the SEC, or (ii) if such a document is a "final official statement", as defined in paragraph (f)(3) of the Rule, available from the MSRB.

Section 3.2. Submission of Information. Annual Financial Information may be provided in one document or multiple documents, and at one time or in part from time to time.

Section 3.3. Material Event Notices. Each notice of a Material Event hereunder shall indicate that it is a notice of a Material Event and shall include the CUSIP numbers of the State or the CUSIP numbers of the Bonds.

Section 3.4 Filing with Certain Dissemination Agents. The State may satisfy its obligations hereunder to file any notice, document or information with a NRMSIR or SID by filing the same with any dissemination agent, including any "central post office" or similar entity, assuming or charged with responsibility for accepting notices, documents or information for transmission to such NRMSIR or SID, to the extent permitted by the SEC or SEC staff or required by the SEC. For this purpose, permission shall be deemed to have been granted by the SEC staff if and to the extent the agent has received an interpretive letter, which has not been revoked, from the SEC staff to the effect that using the agent to transmit information to the NRMSIRs and the SID will be treated for purposes of the Rule as if such information were transmitted directly to the NRMSIRs and the SID.

Section 3.5 Transmission of Information and Notices. Unless otherwise required by law and, in the State's sole determination, subject to technical and economic feasibility, the State shall employ such methods of information and notice transmission as shall be requested or recommended by the recipients of the State's information and notices.

Section 3.6 Fiscal Year.

(a) The State's current fiscal year is July 1 - June 30. The State shall promptly notify (i) each NRMSIR and (ii) the SID of each change in its fiscal year.

(b) The State shall provide Annual Financial Information at least annually notwithstanding any fiscal year longer than 12 calendar months.

ARTICLE IV

Effective Date, Termination, Amendment and Enforcement

Section 4.1. Effective Date; Termination.

(a) This Undertaking shall be effective upon the issuance of the Bonds.

(b) The State's obligations under this Undertaking shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds.

(c) This Undertaking, or any provision hereof, shall be null and void in the event that the State (1) receives an opinion of Counsel to the effect that those portions of the Rule which require this Undertaking, or such provision, as the case may be, do not or no longer apply to the Bonds, whether because such

portions of the Rule are invalid, have been repealed, or otherwise, as shall be specified in such opinion, and (2) delivers copies of such opinion to each NRMSIR and the SID.

Section 4.2. Amendment.

(a) This Undertaking may be amended without the consent of the holders of the Bonds, if all of the following conditions are satisfied: (1) such amendment is made in connection with a change in circumstances that arises from a change in legal (including regulatory) requirements, a change in law (including rules and regulations) or in interpretations thereof, or a change in the identity, nature or status of the State or the type of business conducted thereby, (2) this Undertaking as so amended would have complied with the requirements of the Rule as of the date hereof, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances, (3) the State shall have received an opinion of Counsel to the same effect as set forth in clause (2) above, (4) the State shall have received either an opinion of Counsel or a determination by a person, in each case unaffiliated with the State, to the effect that the amendment does not materially impair the interests of the holders of the outstanding Bonds, and (5) the State shall have delivered copies of such opinion(s) and amendment to each NRMSIR and the SID.

(b) This Undertaking may be amended without the consent of the holders of the Bonds if all of the following conditions are satisfied: (1) an amendment to the Rule is adopted, or a new or modified official interpretation of the Rule is issued, after the effective date hereof which is applicable to this Undertaking, (2) the State shall have received an opinion of Counsel to the effect that performance by the State under this Undertaking as so amended will not result in a violation of the Rule as so amended or officially interpreted and (3) the State shall have delivered copies of such opinion and amendment to each NRMSIR and the SID.

(c) To the extent any amendment to this Undertaking results in a change in the categories or types of financial information or operating data provided pursuant to this Undertaking, the first Annual Financial Information provided thereafter shall include a narrative explanation of the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

(d) If an amendment is made pursuant to Section 4.2(a) hereof to the accounting principles to be followed by the State in preparing its financial statements, the Annual Financial Information for the fiscal year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. Such comparison shall include a qualitative and, to the extent reasonably feasible, quantitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information.

Section 4.3. Contract; Benefit; Third-Party Beneficiaries; Enforcement.

(a) The provisions of this Undertaking shall constitute a contract with and inure solely to the benefit of the holders from time to time of the Bonds, except that beneficial owners of Bonds shall be third-party beneficiaries of this Undertaking and shall be deemed to be holders of Bonds for purposes of Section 4.3(b) hereof. The provisions of this Undertaking shall create no rights in any person or entity except as provided in this subsection (a).

(b) The obligations of the State to comply with the provisions of this Undertaking shall be enforceable by any holder of outstanding Bonds; however, the holders' rights to enforce the provisions of this Undertaking shall be limited solely to a right, by action in mandamus or for specific performance, to compel performance of the State's obligations under this Undertaking.

(c) Any failure by the State to perform in accordance with this Undertaking shall not constitute a default or an event of default under the Bond Resolution or State law and shall not result in any acceleration of payment of the Bonds, and the rights and remedies provided by the Bond Resolution and applicable State law upon the occurrence of such a default or an event of default shall not apply to any such failure.

(d) This Undertaking shall be construed and interpreted in accordance with the laws of the State, and any suits and actions arising out of this Undertaking shall be instituted in a court of competent jurisdiction in the State; provided, however, that to the extent this Undertaking addresses matters of federal securities laws, including the Rule, this Undertaking shall be construed in accordance with such federal securities laws and official interpretations thereof.

Section 4.4. Effective Date. This Undertaking shall be effective upon the issuance and delivery by the State of the Bonds.

STATE OF TENNESSEE

By _____
Mary-Margaret Collier
Assistant Secretary, Funding Board
of the State of Tennessee, *and*
Director, Division of Bond Finance,
State of Tennessee

**PROVISIONS RELATING TO SERIES B BONDS OUTSTANDING
AS VARIABLE RATE BONDS OR FIXED RATE BONDS**

The following is a summary of certain provisions of the Resolution relating to Series B Bonds as Variable Rate Bonds and Fixed Rate Bonds, including certain definitions. **As used in this Appendix F, the term “Bonds” means the Series B Bonds.** This summary is not to be regarded as a full statement of the terms of the Resolution and, accordingly, is qualified by reference thereto and is subject to the full text thereof. Capitalized terms not otherwise defined in this Official Statement or defined in this Appendix F shall have the meanings set forth in the Resolution, copies of which may be obtained from the Division of Bond Finance of the State of Tennessee.

See also “The Bonds – Series B Bonds” in this Official Statement for a description of certain other provisions of the Resolution relating to the Series B Bonds.

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Section 1.1 Definitions. In addition to the words and terms defined in the Resolution, the following words and terms with respect to the Bonds shall have the following meanings unless the context or use indicates another or different meaning or intent (terms defined herein or in the Resolution shall, unless the context requires otherwise, have the meanings given herein with respect to the Bonds outstanding as Variable Rate Bonds or Fixed Rate Bonds, as the case may be):

“Alternate Liquidity Facility” shall mean each replacement letter of credit, line of credit, standby bond purchase agreement or similar agreement entered into and delivered to and accepted by the Paying Agent and Registrar pursuant to the Resolution, as amended, supplemented or extended from time to time.

“Authorized Denomination” shall mean (i) while the interest on the Bonds is calculated at a Daily, Weekly or Monthly Rate, \$100,000 and integral multiples of \$5,000 in excess of \$100,000, and (ii) while the interest on the Bonds is calculated at a Quarterly, Semiannual, Extended or Fixed Rate, \$5,000 and integral multiples thereof.

“Beneficial Owners” shall mean individual purchasers of beneficial ownership interests in the Bonds.

“Bond Counsel” means Hawkins Delafield & Wood LLP or such other nationally recognized bond counsel selected by the State and reasonably satisfactory to the Paying Agent and Registrar.

“Bondholder” or **“Holder”** or **“holder”** or **“Owner”** or **“owner”** of a Bond, or words of like import, shall mean the registered owner of such Bonds.

“Book-Entry-Only System” shall mean a book-entry-only system of registration and transfers of beneficial ownerships of the Bonds.

“Business Day” shall mean a day other than (a) a Saturday, Sunday or day on which banks in the State of New York or banks located in each of the cities in which the principal office of the Paying Agent (including, while the State is the Paying Agent and Registrar, Nashville, Tennessee) and Registrar and the Tender Agent, the Remarketing Agent and the Liquidity Facility Provider, if any, are located are required or authorized by law or executive order to close for business, and (b) a day on which DTC or The New York Stock Exchange is closed.

“Conversion Date” shall mean:

(a) When used with respect to the Fixed Rate, the date on which the Fixed Rate becomes effective pursuant to Section 1.2(m) of this Appendix F; and

(b) When used with respect to any particular Variable Rate Period, the date on which such Variable Rate Period first becomes effective pursuant to Section 1.2(j) of this Appendix F.

“Daily Rate” shall mean the per annum interest rate on the Bonds for a Daily Rate Period pursuant to Section 1.2(c) of this Appendix F.

“Daily Rate Period” shall mean, while the interest rate on the Bonds is determined at the Daily Rate, the period commencing on each Business Day to but excluding the following Business Day.

“DTC” shall mean The Depository Trust Company.

“DTC Indirect Participant” shall mean an indirect participant in DTC.

“DTC Participant” shall mean a direct participant in DTC.

“Event of Termination” shall have the meaning given such term in the Liquidity Facility.

“Extended Rate” shall mean the per annum interest rate on the Bonds for an Extended Rate Period pursuant to Section 1.2(h) of this Appendix F.

“Extended Rate Period” shall mean, while the interest rate on the Bonds is determined at the Extended Rate, (i) the Initial Extended Rate Period, (ii) the period from and including the Extended Rate Conversion Date, and (iii) the period from and including the first Business Day of the calendar month following the last day of the prior Extended Rate Period, (iv) in each case (other than the Initial Extended Rate Period) extending for a period of one year or integral multiple of six months in excess of one year set by the State or, if not set by the State, for a period of one year, ending on a day which is the last day preceding the first Business Day of a calendar month.

“Favorable Opinion” shall mean a written opinion of Bond Counsel, in form and substance satisfactory to the Paying Agent and Registrar, and except as may be otherwise specifically set forth in the Resolution, to the effect that the action proposed to be taken is authorized or permitted by the laws of the State and the Resolution.

“Fitch” shall mean Fitch Ratings or its successor.

“Fixed Rate” shall mean the per annum interest rate on the Bonds determined pursuant to Section 1.2(p) of this Appendix F.

“Fixed Rate Period” shall mean the period of time during which the interest rate on the Bonds is determined at a Fixed Rate.

“Initial Extended Rate Period” shall mean the period from and including the dated date of the Bonds to and including the last day of February, 2010.

“Interest Payment Date” shall mean, with respect to the Bonds:

(i) when the interest rate on the Bonds is determined at the Daily, Weekly or Monthly Rate, the first Business Day of each calendar month;

(ii) when the interest rate on the Bonds is determined at the Quarterly Rate, the first Business Day of the third calendar month following the Quarterly Rate Conversion Date and subsequently the first Business Day of each third calendar month thereafter;

(iii) when the interest rate on the Bonds is determined at the Semiannual Rate, the first Business Day of the sixth month following the Semiannual Rate Conversion Date and subsequently the first Business Day of each sixth calendar month thereafter;

(iv) when the interest rate on the Bonds is determined at the Extended Rate, September 1, 2004, or the first Business Day of the sixth month following any Extended Rate Conversion Date, and subsequently the first Business Day of each sixth calendar month thereafter;

(v) when the interest rate on the Bonds is determined at the Fixed Rate, each March 1 and September 1 after the Fixed Rate Conversion Date;

(vi) when the Bonds constitute Provider Bonds, each date on which interest on the Provider Bonds is due and payable in accordance with the provisions of the Liquidity Facility or any reimbursement or similar agreement entered into between the State and the Liquidity Provider;

(vii) with respect to any Bonds which are to be redeemed prior to maturity, any date on which such redemption is made; and

(viii) with respect to any Bonds, the Maturity Date.

“LIBOR” shall mean the London Interbank Offering Rate.

“Liquidity Facility” shall mean a letter of credit, line of credit, standby purchase agreement or similar agreement entered into pursuant to the Resolution, and any Alternate Liquidity Facility delivered to or entered into and accepted by the Paying Agent and Registrar, in each case as amended, supplemented or extended from time to time.

“Liquidity Provider” shall mean the provider of a Liquidity Facility including its permitted assignees and successors.

“Maturity Date” shall mean March 1, 2029.

“Maximum Rate” shall mean, with respect to the Bonds, the lesser of 12% or the maximum rate of interest allowable by Section 47-14-103, Tennessee Code Annotated, or other applicable State law; provided, however, that with respect to Provider Bonds, Maximum Rate shall mean the maximum rate of interest allowable by Section 47-14-103, Tennessee Code Annotated, or other applicable State law, or otherwise as may be specified in the related Liquidity Facility.

“Monthly Rate” shall mean the per annum interest rate on the Bonds determined for a Monthly Rate Period pursuant to Section 1.2(e) of this Appendix F.

“Monthly Rate Period” shall mean, while the interest rate on the Bonds is determined at the Monthly Rate, the period commencing on the Monthly Rate Conversion Date on the Bonds, and on the first Business Day of each month thereafter, to but excluding the first Business Day of the following month.

“Moody’s” shall mean Moody’s Investors Service, Inc., or its successor.

“Notice Termination Date” shall mean the date upon which the Liquidity Facility is to terminate after notice from the Liquidity Provider, which date must be at least thirty (30) days after the date on which the Paying Agent and Registrar and Tender Agent receive notice from the Liquidity Provider stating that as a result of an Event of Termination under the Liquidity Facility that permits such termination, the Liquidity Provider in accordance with the provisions of the Liquidity Facility has elected to terminate the Liquidity Facility and stating the date of termination, and any termination date under an Alternate Liquidity Facility pursuant to which a similar notice of termination is given.

“Paying Agent and Registrar” shall have the meaning given to such term in the Resolution, and initially shall be the State (acting through the State Treasurer or State Comptroller or both) or any successor or successors appointed in accordance with the Resolution.

“Person” shall mean any individual, corporation, partnership, joint venture, association, joint stock company, limited liability company, trust, unincorporated organization, or other entity or organization, including a government or any political subdivision or agency or instrumentality thereof, unless the context shall otherwise indicate.

“Provider Bonds” shall mean Bonds purchased with funds made available under or pursuant to the Liquidity Facility, registered in the name of the Liquidity Provider or its nominee, designee or assignee and held by the Paying Agent and Registrar in trust for the benefit of the Liquidity Provider or its nominee, designee or assignee.

“Provider Rate” shall mean the interest rate which Provider Bonds bear from time to time, as determined in the accordance with the provisions of the Liquidity Facility or any reimbursement or similar agreement entered into between the State and the Liquidity Provider, but not in excess of the Maximum Rate.

“Purchase Date” shall mean the date upon which the Tender Agent is obligated to purchase a Bond or Bonds pursuant to Sections 1.4, 1.5, 1.6, 1.9 and 1.10 of this Appendix F.

“Purchase Price” of any Bond required to be purchased by the Tender Agent pursuant to Sections 1.4, 1.5, 1.6, 1.9 and 1.10 of this Appendix F shall mean an amount equal to the principal amount thereof plus, if the Purchase Date is other than an Interest Payment Date, the accrued interest thereon at the rate applicable to the Bond from the most recent Interest Payment Date up to but excluding the Purchase Date.

“Quarterly Rate” shall mean the per annum interest rate on the Bonds determined for Quarterly Rate Period pursuant to Section 1.2(f) of this Appendix F.

“Quarterly Rate Period” shall mean, while the interest rate on the Bonds is determined at the Quarterly Rate, the period commencing on the Quarterly Rate Conversion Date for the Bonds, and on the first Business Day of each third calendar month thereafter, to but excluding the first Business Day of the third calendar month thereafter.

“Rate Period” or **“Period”** shall mean, when used with respect to any particular rate of interest on the Bonds (whether a Daily, Weekly, Monthly, Quarterly, Semiannual, Extended or Fixed Rate), the period during which such rate of interest will remain in effect pursuant to this Appendix F, as the case may be.

“Rating Agency” shall mean each of Fitch, Moody’s, S&P, and any other nationally recognized rating service which, at the request of the State, shall have provided a rating on any outstanding Bonds.

“Record Date” shall mean, with respect to each Interest Payment Date, (i) the Business Day immediately prior to such Interest Payment Date in the case of the Daily and Weekly Rate Periods, (ii) the last Business Day at least 5 days prior to such Interest Payment Date in the case of the Monthly Rate Period, (iii) the 15th day (whether or not a Business Day) of the calendar month immediately preceding such Interest Payment Date in the case of the Quarterly, Semiannual, Extended Rate or Fixed Rate Periods, and (iv) as provided by the Liquidity Facility in the case of Provider Bonds.

“Remarketing Agent” shall mean any remarketing agent appointed by the State pursuant to the Resolution.

“Remarketing Agreement” shall mean the Remarketing Agreement between the State and the Remarketing Agent.

“S&P” shall mean Standard & Poor’s Ratings Services, a division of The McGraw Hill Companies, Inc., or its successor.

“Semiannual Rate” shall mean the per annum interest rate on the Bonds determined for a Semiannual Rate Period pursuant to Section 1.2(g) of this Appendix F.

“Semiannual Rate Period” shall mean, while the interest rate on the Bonds is determined at the Semiannual Rate, the period commencing on the Semiannual Rate Conversion Date, and from and including the first Business Day of each sixth calendar month thereafter, to but excluding the first Business Day of the sixth calendar month thereafter.

“Special Termination Event” shall mean an Event of Termination under the Liquidity Facility that permits the Liquidity Provider to immediately terminate or suspend its obligation to purchase Bonds tendered for purchase, and any event under an Alternate Liquidity Facility which results in the immediate termination or suspension of an alternate liquidity provider’s obligations to purchase Bonds.

“Tender Agent” shall mean the Tender Agent or any successor or successors appointed in accordance with the Resolution.

“Variable Rate” shall mean, as the context requires, the Daily, Weekly, Monthly, Quarterly, Semiannual or Extended Rate applicable to the Bonds.

“Variable Rate Period” shall mean, as the context requires, any or all of the Daily Rate Period, Weekly Rate Period, Monthly Rate Period, Quarterly Rate Period, Semiannual Rate Period or Extended Rate Period applicable to the Bonds.

“Weekly Rate” shall mean the per annum interest rate on the Bonds determined for a Weekly Rate Period pursuant to Section 1.2(d) of this Appendix F.

“Weekly Rate Period” shall mean, while the interest rate on the Bonds is determined at the Weekly Rate, the period from and including Thursday of each week to but excluding Thursday of the following week, except that in the case of a conversion to a Weekly Rate Period from a different Variable Rate Period, the initial Weekly Rate Period shall be from and including the Weekly Rate Conversion Date to but excluding Thursday of the following week.

Section 1.2 General Terms and Provisions.

(a) Terms of Variable Rate Bonds. The Bonds (A) shall be payable as to interest on each Interest Payment Date established therefor at the rate per annum determined as provided in this Section 1.2, and (B) shall be subject to redemption, to optional and mandatory tender for purchase, and to remarketing, all as provided in the Resolution. While interest on the Bonds is determined at the Daily Rate, Weekly Rate, Monthly Rate and Quarterly Rate, such interest will be calculated based on the actual days elapsed and a year of 365 or 366 days, as applicable, and while interest on the Bonds is determined at the Semiannual Rate, Extended Rate or Fixed Rate, such interest will be calculated based on a year of 360 days consisting of twelve 30 day months.

(b) Variable Rate; Determination by Remarketing Agent; Notice of Rates Determined. The Bonds shall initially bear interest at Extended Rates for Extended Rate Periods until converted to another Rate Period as provided herein. Subject to the further provisions of this Section 1.2 with respect to particular Variable Rates or conversions between Rate Periods, and subject to the provisions of the Bonds, the Variable Rate to be applicable to Bonds during any Variable Rate Period shall be determined by the Remarketing Agent as provided in this Section 1.2 and notice thereof shall be given as follows:

(i) Notice of each preliminary Quarterly, Semiannual and Extended Rate and Extended Rate Period and of each Variable Rate shall be given as follows:

(A) By the Remarketing Agent to the Paying Agent and Registrar and the Tender Agent by telephone (followed by notice in writing by an authorized officer of the Remarketing Agent) not later than 5:00 p.m., New York City time (10:00 a.m., New York City time, with respect to Daily Rates) on the date of determination; and

(B) On the last Business Day of each month or more frequently upon any Liquidity Provider’s written request, the Tender Agent shall provide written notice thereof to the Liquidity Provider.

Notice of each preliminary Quarterly, Semiannual and Extended Rate and Extended Rate Period, and of each Monthly, Quarterly, Semiannual and Extended Rate and Extended Rate Period, shall be given by the Paying Agent and Registrar by sending notice in writing to the Owners of the Bonds and the Tender Agent not later than 5:00 p.m., New York City time, on the third Business Day following the date of determination. In the case of an Extended Rate Period with a duration of more than one year, such notice also shall include or be accompanied by notice of the optional redemption provisions established pursuant to the Resolution. The Tender Agent shall inform the Owners of the Bonds and the Paying Agent and Registrar of the Daily and Weekly Rates upon request.

(ii) The preliminary Quarterly, Semiannual and Extended Rate or the Variable Rate so to be determined shall be the lowest rate of interest which, in the judgment of the Remarketing Agent, would cause the Bonds to have a market value equal to the principal amount thereof, plus the accrued interest thereon, under prevailing market conditions as of the date of determination of such preliminary Quarterly, Semiannual and Extended Rate or Variable Rate. The preliminary Quarterly, Semiannual and Extended Rate is intended to serve only as an indication of the lowest interest rate that would cause the Bonds to have a market value equal to par under

market conditions on the date on which such preliminary Quarterly, Semiannual and Extended Rate is determined. The Quarterly, Semiannual and Extended Rate determined after the preliminary Quarterly, Semiannual and Extended Rate is determined may be higher, lower or the same as such preliminary Quarterly, Semiannual and Extended Rate. Notwithstanding the foregoing, in no event shall the preliminary Quarterly, Semiannual and Extended Rate or the Variable Rate for any Variable Rate Period exceed the Maximum Rate.

(iii) All determinations of Variable Rates pursuant to this Section 1.2 shall be conclusive and binding upon the State, the Paying Agent and Registrar, the Tender Agent, the Liquidity Provider, and the Owners of the Bonds. The State, the Paying Agent and Registrar, the Tender Agent and the Remarketing Agent shall not be liable to the Owner of any Bond for failure to give any notice required above or for failure of the Owner of any Bond to receive any such notice.

(c) Daily Rates.

(i) The Daily Rate Periods shall be from each Business Day to but excluding the following Business Day.

(ii) The Daily Rate for each Daily Rate Period shall be determined by the Remarketing Agent not later than 10:00 a.m., New York City time, on the commencement date of the Daily Rate Period to which it relates.

(d) Weekly Rates.

(i) Weekly Rate Periods shall be from and including Thursday of each week to but excluding Thursday of the following week, except that in the case of a conversion to a Weekly Rate Period from a different Variable Rate Period, the initial Weekly Rate Period for the Bonds shall be from and including the Weekly Rate Conversion Date to but excluding Thursday of the following week.

(ii) The Weekly Rate for each Weekly Rate Period shall be determined not later than 4:00 p.m., New York City time, on Wednesday or, if such Wednesday is not a Business Day, the last Business Day which is immediately prior to the commencement date of the Weekly Rate Period to which it relates.

(e) Monthly Rates.

(i) Monthly Rate Periods shall be (A) from and including the Monthly Rate Conversion Date for the Bonds and from and including the first Business Day of each calendar month thereafter (B) to but excluding the first Business Day of the following month.

(ii) The Monthly Rate for each Monthly Rate Period shall be determined not later than 4:00 p.m., New York City time, on the Business Day immediately preceding the commencement date of such period.

(f) Quarterly Rates.

(i) Quarterly Rate Periods shall be (A) from and including the Quarterly Rate Conversion Date for the Bonds and from and including the first Business Day of each third calendar month thereafter (B) to but excluding the first Business Day of the third calendar month thereafter.

(ii) The Quarterly Rate for each Quarterly Rate Period shall be determined as follows:

(A) A preliminary Quarterly Rate for each Quarterly Rate Period shall be determined not later than 4:00 p.m., New York City time, on the last Business Day which is at least 15 days preceding the commencement date of such period; and

(B) The actual Quarterly Rate for each Quarterly Rate Period shall be determined not later than 4:00 p.m., New York City time, on the Business Day immediately preceding the commencement date of such period.

(g) Semiannual Rates.

(i) Semiannual Rate Periods shall be (A) from and including the Semiannual Rate Conversion Date for the Bonds and from and including the first Business Day of each sixth calendar month thereafter (B) to but excluding the first Business Day of the sixth month thereafter.

(ii) The Semiannual Rate for each Semiannual Rate Period shall be determined as follows:

(A) A preliminary Semiannual Rate for each Semiannual Rate Period shall be determined not later than 4:00 p.m., New York City time, on the last Business Day which is at least 30 days immediately preceding the commencement date of such period;

(B) The actual Semiannual Rate for each Semiannual Rate Period shall be determined not later than 4:00 p.m., New York City time, on the Business Day immediately preceding the commencement date of such period.

(h) Extended Rates.

(i) Extended Rate Periods shall be (A) the Initial Extended Rate Period, (B) from and including the Extended Rate Conversion Date for the Bonds, and (C) from and including the first Business Day of the calendar month following the last day of the prior Extended Rate Period, (D) in each case extending for a period of one year or integral multiples of six months in excess of one year set by the State or, if not set by the State, for a period of one year, ending on a day which is the last day preceding the first Business Day of a calendar month.

(ii) The Extended Rate for each Extended Rate Period after the Initial Extended Rate Period shall be determined as follows:

(A) A preliminary Extended Rate for each Extended Rate Period shall be determined not later than 4:00 p.m., New York City time, on the last Business Day which is at least 30 days immediately preceding the commencement date of such period;

(B) The actual Extended Rate for each Extended Rate Period shall be determined not later than 4:00 p.m., New York City time, on the Business Day immediately preceding the commencement date of such period.

(i) Limitation on Rate Periods. None of the Variable Rate Periods may extend beyond the scheduled expiration date of the applicable Liquidity Facility, provided that a Liquidity Facility is required to be maintained during such Variable Rate Period. Subject to Section 2(e) of the Resolution, no Liquidity Facility is required to be maintained during the Initial Extended Rate Period.

(j) Conversion between Variable Rate Periods. At the option of the State, the Bonds may be converted from one Variable Rate Period to another as provided in this paragraph (j). The Conversion Date shall be an Interest Payment Date for the Variable Rate Period from which the conversion is to be made; provided, however, that in the case of a conversion from an Extended Rate Period, the Conversion Date shall be limited to an Interest Payment Date on which a new Extended Rate Period for the Bonds would otherwise have commenced pursuant to Section 1.2(h) of this Appendix F. At the direction of the State, the Remarketing Agent shall give written notice of any conversion pursuant to this paragraph (j) to the Paying Agent and Registrar, the Tender Agent, the State and the Liquidity Provider not less than five Business Days prior to the date on which the Tender Agent is required to notify the Owners of the conversion in the manner provided in this paragraph (j). Such notice shall specify the Conversion Date and the Rate Period to which the conversion will be made. Not less than 15 days prior to any Conversion Date, the Tender Agent shall mail or cause the Paying Agent and Registrar to mail a written notice of the conversion to the

State, the Liquidity Provider and all of the Owners of the Bonds. Such notice shall set forth (A) the information contained in the notice from the Remarketing Agent pursuant to this paragraph (j), (B) the Interest Payment Dates for the new Rate Period, (C) the dates on which the Remarketing Agent will determine and the Tender Agent will notify the Owners of the preliminary Variable Rate (if applicable) and the Variable Rate for the Variable Rate Period commencing on the Conversion Date, and (D) the matters required to be stated pursuant to Section 1.5(b) of this Appendix F with respect to purchases of Bonds which are governed by such Section.

(k) Determination of Variable Rate Effective on Conversion Date. The preliminary Variable Rate (if applicable) and the Variable Rate for the Variable Rate Period commencing on the Conversion Date shall be determined by the Remarketing Agent in the manner and on the dates provided in this Section 1.2. In addition to determining the Variable Rate for the Rate Period to which conversion is to be made, the Remarketing Agent shall determine a Weekly Rate at the time specified in Section 1.2(d), and give notice thereof to the Tender Agent, the State and the Paying Agent and Registrar, which Weekly Rate shall take effect, if needed, pursuant to clause (l) below.

(l) Conditions on which Conversion Ineffective. Notwithstanding the delivery of notice of conversion pursuant to paragraph (j) above, conversion to a new Variable Rate Period shall not take effect as to the Bonds if:

(i) The Remarketing Agent fails to determine a Variable Rate for the Rate Period to which the conversion is to be made;

(ii) Any notice required by Section 1.2(j) of this Appendix F is not given when required;

(iii) There is not delivered to the State, the Remarketing Agent, the Liquidity Provider and the Paying Agent and Registrar a Favorable Opinion dated as of the Conversion Date;

(iv) Such notice of conversion is rescinded by the State by written notice of such rescission to the Paying Agent and Registrar and the Remarketing Agent, which written notice is delivered prior to the applicable Conversion Date. If the Paying Agent and Registrar receives notice of such rescission at least 10 days prior to the proposed Conversion Date, then such notice of conversion shall be of no force and effect. If the Paying Agent and Registrar receives notice of such rescission less than 10 days prior to the proposed Conversion Date, then the Bonds shall automatically adjust to a Weekly Rate Period. Any purchases of Bonds scheduled or required to take place on the proposed effective date of any Rate Period (being also the effective date of the automatic adjustment to a Weekly Rate Period as in this Section 1.2(l) provided) shall take place on such date. No Favorable Opinion shall be required in connection with any automatic adjustment to a Weekly Rate Period as in this Section 1.2(l) provided; or

(v) There is not delivered to the Paying Agent and Registrar and the Remarketing Agent written evidence from each Rating Agency to the effect that any such conversion to a Quarterly Rate, Semiannual Rate or Extended Rate will not, of itself, cause a reduction or withdrawal of any rating (other than a short term rating) then assigned to the Bonds, or confirming any such then-existing rating giving effect to such conversion; provided, however, that (i) a reduction in rating resulting solely from provision of an Alternate Liquidity Facility shall not render such conversion ineffective if the Alternate Liquidity Facility complies with the requirements of this Series Certificate or (ii) a reduction in rating resulting solely from failure to provide a Liquidity Facility for the proposed Rate Period shall not render such conversion ineffective if the Bonds shall otherwise comply with the requirements of the Resolution.

In any such event, except as specifically provided in (iv) above in the case of a rescission at least 10 days prior to the proposed Conversion Date, the Bonds which were to be converted shall automatically be converted to a Weekly Rate Period on the date such conversion was to be made; provided, however, that any mandatory or optional tender for purchase on the Conversion Date shall nevertheless be carried out. No cancellation of a conversion pursuant to this Section 1.2(l) shall constitute an event of default under the Resolution. Upon the occurrence of an event described in (i) above, the Weekly Rate for the Bonds shall be the per annum rate of interest determined on each Wednesday (or if such day is not a Business Day, the immediately preceding Business Day) by the Paying Agent

and Registrar which is equal to the lesser of the Maximum Rate or a rate equal to one-month LIBOR plus 25 basis points.

(m) Conversion to Fixed Rate. The Bonds in a Variable Rate Period shall be converted to bear interest at a Fixed Rate upon request of the State as provided in this paragraph (m). The Fixed Rate Conversion Date shall be:

(i) In the case of a conversion from a Variable Rate Period other than an Extended Rate Period, an Interest Payment Date for the Bonds on which interest is payable for the Variable Rate Period from which the conversion is to be made; and

(ii) In the case of a conversion from an Extended Rate Period, an Interest Payment Date for the Bonds on which a new Extended Rate Period would otherwise have commenced pursuant to Section 1.2(h) of this Appendix F.

Not less than 45 days (or such shorter period approved by the parties to receive the same) prior to the Fixed Rate Conversion Date, the State shall give written notice to the Paying Agent and Registrar, the Tender Agent, the Remarketing Agent and the Liquidity Provider setting forth (A) the election to convert the Bonds to a Fixed Rate, (B) the proposed Fixed Rate Conversion Date and (C) that the Liquidity Facility, if any, will terminate on the Fixed Rate Conversion Date.

(n) Preliminary Determination of Terms of Bonds Converted to Fixed Rate Bonds. The Remarketing Agent shall make a preliminary determination of the Fixed Rate or Fixed Rates for the Bonds and the maturities of the Bonds in the same manner as is provided for the final determination of rates pursuant to Section 1.2(p) of this Appendix F. Such preliminary determination shall be made on a Business Day which is at least 35 days prior to the Fixed Rate Conversion Date. On the date of the preliminary determination, the Remarketing Agent shall notify the Tender Agent and the Tender Agent shall notify the State and the Paying Agent and Registrar, by telephone (promptly confirmed in writing), telegram, telecopy, telex or other similar means of communication of the preliminary Fixed Rate or Fixed Rates so determined.

(o) Notice of Conversion to Fixed Rate. The Tender Agent shall mail or cause the Paying Agent and Registrar to mail a notice of the proposed conversion to the State, the Paying Agent and Registrar, the Liquidity Provider and the Owners of all Bonds to be converted. Such notice shall be mailed not less than 30 days prior to the proposed Fixed Rate Conversion Date. Such notice shall set forth the proposed Fixed Rate Conversion Date, shall set forth or be accompanied by notice of the optional redemption provisions established pursuant to the Resolution, and shall state:

(i) that the Bonds are subject to mandatory tender for purchase (without the right to retain) on the Fixed Rate Conversion Date at the Purchase Price;

(ii) the time at which the Bonds are to be tendered for purchase; and

(iii) that the Bonds shall be deemed purchased on the Fixed Rate Conversion Date and thereafter the Owner shall have no further rights hereunder except to receive such Purchase Price.

(p) Terms of Fixed Rate Bonds; Determination of Fixed Rate. The Remarketing Agent shall determine the Fixed Rate or Fixed Rates for the Bonds by not later than 3:30 p.m., New York City time, on the last Business Day that is at least 5 days prior to the Fixed Rate Conversion Date for the Bonds. The Fixed Rate or Fixed Rates shall be the lowest rate or rates of interest per annum (not in excess of the maximum rate of interest allowed by law) which, in the judgment of the Remarketing Agent as of the date of determination and under prevailing market conditions, would cause the Fixed Rate Bonds to have a market value equal to the principal amount thereof, plus the accrued interest thereon. If necessary or desirable to achieve the lowest Fixed Rate or Fixed Rates on the Bonds, the Remarketing Agent may determine that some or all of the Bonds which are term bonds shall be converted to serial bonds maturing in years for which mandatory sinking fund redemptions have been established pursuant to Section 301 of this Series Certificate and maturing in aggregate principal portions that correspond to such mandatory sinking fund redemptions. Not later than 4:00 p.m., New York City time, on the date of

determination of the Fixed Rate, the Remarketing Agent shall notify the Tender Agent of the Fixed Rate or Fixed Rates and of any serialization of term maturities of the Bonds by telephone (promptly confirmed in writing). Such determination shall be conclusive and binding upon the State, the Paying Agent and Registrar, the Tender Agent and the Owners of the Bonds. The Tender Agent shall make such Fixed Rate and serialization of term maturities of the Bonds available upon request by telephone (promptly confirmed in writing), telegram, telecopy, telex or other similar communication to the State and the Paying Agent and Registrar. In addition to determining a Fixed Rate, the Remarketing Agent shall determine a Weekly Rate pursuant to Section 1.2(d) of this Appendix F and give notice thereof to the Tender Agent and the Paying Agent and Registrar, which Weekly Rate shall take effect if needed pursuant to Section 1.2(q) of this Appendix F.

(q) Conditions on which Conversion to Fixed Rate Ineffective. Notwithstanding the delivery of notice of a Fixed Rate conversion pursuant to Section 1.2(o) of this Appendix F, conversion of Bonds to a Fixed Rate Period shall not take effect if:

(i) The State withdraws such notice of conversion not later than the Business Day preceding the date on which the Fixed Rate is to be determined;

(ii) The Remarketing Agent fails to determine the Fixed Rate;

(iii) Any notice required by Section 1.2(o) of this Appendix F is not given when required;

(iv) There is not delivered to the State, the Remarketing Agent, the Liquidity Provider and the Paying Agent and Registrar a Favorable Opinion dated as of the Conversion Date; or

(v) Upon the conversion, any Fixed Rate Bonds would be Provider Bonds, unless the Liquidity Provider consents.

In any of such events, the Bonds shall automatically be converted to a Weekly Rate for a Weekly Rate Period which shall commence on the date the Fixed Rate conversion was to be made; provided, however, that the mandatory tender for purchase pursuant to Sections 1.6 and 1.9 of this Appendix F shall nevertheless be carried out if notice of the Fixed Rate conversion had been given to the Owners of the Bonds. Withdrawal of a conversion notice shall be given by the State to the Paying Agent and Registrar, the Tender Agent, the Remarketing Agent and the Liquidity Provider, by telephone, promptly confirmed in writing. No cancellation of a Fixed Rate conversion pursuant to this subsection shall constitute an Event of Default hereunder. If the Bonds are converted to a Weekly Rate, and the Remarketing Agent fails to set a Weekly Rate, the Weekly Rate shall be the per annum rate of interest determined on each Wednesday (or if such day is not a Business Day, the immediately preceding Business Day) by the Paying Agent and Registrar which is equal to the lesser of the Maximum Rate or a rate equal to one-month LIBOR plus 25 basis points.

(r) Effect of Conversion to Fixed Rate. Once the State has effectively exercised its option to convert the Bonds to a Fixed Rate pursuant to this Section 1.2, the State shall not have the option to convert the Bonds to any other Rate Period, and the Bonds shall no longer be payable from or secured by the Liquidity Facility or be subject to tender for purchase.

(s) Provider Bonds. Notwithstanding anything to the contrary contained in this Series Certificate, Provider Bonds shall bear interest at the Provider Rate payable on Interest Payment Dates, all in accordance with the provisions of the Liquidity Facility or any reimbursement or similar agreement entered into between the State and the Liquidity Provider. Bonds which are no longer Provider Bonds shall not bear interest at the Provider Rate.

Section 1.3 Redemption Dates and Prices. The Bonds that are Variable Rate Bonds or Fixed Rate Bonds may be called for redemption by the State as provided in the Resolution.

Section 1.4 Optional Tenders by Owners During Variable Rate Periods.

(a) Purchase Dates. During any Variable Rate Period a Beneficial Owner of the Bonds (other than Provider Bonds) may elect to have its Bonds (or portions thereof in Authorized Denominations) purchased at the Purchase Price, on the following Purchase Dates by causing the DTC Direct Participant through whom such Beneficial Owner owns such Bond to give the following irrevocable telephonic or written notices meeting the further requirements of subsection (b) of this Section 1.4 and upon transfer on the registration books of DTC on the same day such notice is given of the beneficial ownership interest in such Bonds to the account of the Paying Agent and Registrar, “free delivery” for settlement on the Purchase Date:

(i) While interest on the Bonds is determined at Daily Rates, Bonds may be tendered for purchase on any Business Day upon telephonic notice of tender given to the Tender Agent and the Remarketing Agent not later than 10:30 a.m., New York City time, on the Purchase Date;

(ii) While interest on the Bonds is determined at Weekly Rates, Bonds may be tendered for purchase on any Business Day upon delivery of telephonic, facsimile or e-mail notice of tender to the Tender Agent and the Remarketing Agent not later than 5:00 p.m., New York City time, on a Business Day not less than 7 days prior to the Purchase Date;

(iii) While interest on the Bonds is determined at Monthly, Quarterly or Semiannual Rates, Bonds may be tendered for purchase on any Interest Payment Date upon delivery of a written notice of tender to the Tender Agent not later than 5:00 p.m., New York City time, on a Business Day which is not less than 7 days prior to the Interest Payment Date while interest is determined at Monthly and Quarterly Rates, or 15 days prior to the Interest Payment Date while interest is determined at Semiannual Rates; and

(iv) While interest on the Bonds is determined at Extended Rates, Bonds may be tendered for purchase on the commencement date of any Extended Rate Period (other than the Extended Rate Conversion Date) upon delivery of a written notice of tender to the Tender Agent not later than 5:00 p.m., New York City time, on a Business Day which is not less than 15 days prior to the Purchase Date.

(b) Notice of Tender. Each notice of tender:

(i) shall, in the case of a written notice be delivered to the Tender Agent and, while interest on the Bonds is determined at Weekly Rates, a copy thereof delivered to the Remarketing Agent, at its principal office and containing the information required in the form attached as Appendix 2 to this Appendix F;

(ii) shall state, whether delivered in writing or by telephone (A) the principal of the Bonds or portion thereof to be purchased, (B) that the Owner irrevocably demands purchase of such principal or portion thereof, (C) the date on which such principal or portion thereof is to be purchased, (D) payment instructions, and (E) the DTC identification number of such DTC Direct Participant; and

(iii) shall automatically constitute, whether delivered in writing or by telephone (A) an irrevocable offer to sell the principal of the Bond or portion thereof to which the notice relates on the Purchase Date to any purchaser selected by the Remarketing Agent, at the Purchase Price, (B) an irrevocable authorization and instruction to the Paying Agent and Registrar to effect transfer of such principal or portion thereof upon payment of such price to the Paying Agent and Registrar on the Purchase Date, (C) an irrevocable authorization and instruction to the Tender Agent to effect the exchange of the Bond to be purchased in whole or in part for other Bonds of the same maturity in an equal aggregate principal amount so as to facilitate the sale of the principal or portion thereof, and (D) an acknowledgment that such Owner will have no further rights with respect to the principal or interest of the Bond or portion thereof upon payment of the Purchase Price by the Paying Agent and Registrar on the Purchase Date to the DTC Direct Participant from whom the notice of tender is received, except for the right of such Owner to receive such Purchase Price upon surrender of such Bond to the Tender Agent.

The determination of the Tender Agent as to whether a notice of tender has been properly delivered pursuant to the foregoing shall be conclusive and binding upon the Owner. The Tender Agent shall hold beneficial ownership interests of the principal and interest of Bonds delivered to it pursuant to this Section 1.4 pending

settlement in trust for the benefit of the DTC Direct Participant from whom the beneficial ownership interests in the principal and interest of such Bonds are received and shall remit any payment of the interest received with respect to such Bonds for the period prior to the Purchase Date to such DTC Direct Participant.

(c) Bonds to be Remarketed. Not later than 4:30 p.m., New York City time, on the Business Day immediately following the date of receipt of any notice of tender (or immediately upon such receipt, in the case of Bonds bearing interest at Daily Rates), the Tender Agent shall notify the Paying Agent and Registrar and the Remarketing Agent of the principal of Bonds or portions thereof to be tendered and remarketed and the date they are to be tendered and remarketed. Such notices shall be given by telephone, telegram, telecopy, telex or other similar communication and shall be promptly confirmed in writing.

(d) Remarketing of Tendered Bonds. The Remarketing Agent shall offer for sale and use its best efforts to find purchasers for all portions of the Bonds or portions thereof properly tendered. All Bonds shall be at all times remarketed at a price equal to the principal amount thereof, plus the interest thereon accrued up to the remarketing date. Notwithstanding the foregoing, the Remarketing Agent shall not offer for sale any portion of Bonds if notice of (i) any optional or mandatory prepayment, (ii) any conversion from one Variable Rate Period to another or to a Fixed Rate Period has been given to the Owners of the Bonds pursuant to the provisions of this Series Certificate, or (iii) any financial defeasance has occurred, unless the Remarketing Agent has advised the Person in writing to whom the offer is made of such occurrence and the effect of the same on the rights of such Owners including, but not limited to, the rights of such Owners to tender their Bonds, as described in the conversion notice from the Tender Agent to the Owners of the Bonds.

Section 1.5 Mandatory Tenders Upon Variable Rate Conversion.

(a) Purchase Dates. In the case of any conversion from one Variable Rate Period to another Variable Rate Period (except a conversion between a Daily Rate Period and a Weekly Rate Period), Bonds to be converted are subject to mandatory tender for purchase on the Conversion Date at the Purchase Price.

(b) Notice to Owners. Any notice of a conversion given to Bondholders pursuant to Section 1.2(j) of this Appendix F shall, in addition to the requirements of such Section, specify that the Bonds to be converted will be subject to mandatory tender for purchase on the Conversion Date and the time at which Bonds are to be tendered for purchase.

(c) Remarketing. At or before 4:00 p.m., New York City time, on the fifth Business Day immediately preceding the conversion to a Daily, Weekly or Monthly Rate Period or on the seventh calendar day (or, if such day is not a Business Day, on the next succeeding Business Day) preceding the conversion to a Quarterly Rate Period or on the fifteenth calendar day (or, if such day is not a Business Day, on the next succeeding Business Day) preceding the conversion to a Semiannual or Extended Rate Period, the Paying Agent and Registrar shall notify the Tender Agent, the Liquidity Provider and the Remarketing Agent, by telephone, telegram, telecopy, telex or other similar communication, of the aggregate principal amount of Bonds to be tendered for purchase on the Conversion Date. The Remarketing Agent shall offer for sale and use its best efforts to find purchasers for the Bonds to be tendered. All Bonds shall be at all times remarketed at a price equal to the principal amount thereof, plus the interest accrued up to the remarketing date.

Section 1.6 Mandatory Tenders Upon Expiration, Substitution or Termination of Liquidity Facility and Division Into Subseries.

(a) Purchase Dates. Prior to the Fixed Rate Conversion Date of the interest on the Bonds, the Bonds shall be subject to mandatory tender for purchase at the Purchase Price:

(i) on a Substitution Date; or

(ii) on a Business Day which is at least five days prior to the expiration of the Liquidity Facility (other than when the State is not required to maintain a Liquidity Facility because the Bonds receive a rating from each Rating Agency in the highest short term category (without regard to gradations within such category), which rating is not based on a Liquidity Facility); or

(iii) on a Business Day which is at least five days prior to a Notice Termination Date; or

(iv) on the effective date of any division of Bonds into subseries as permitted by the Resolution (but this clause (iv) shall not apply to any subseries not being further divided into additional subseries).

(b) Notice to Owners. Notice of mandatory tender of Bonds shall be given by mail by the Paying Agent and Registrar to the Owners of such Bonds by first class mail not less than 30 days prior to the mandatory tender date. A copy of such notice shall be sent to the State and the Paying Agent and Registrar. Notice having been so given, such mandatory tender shall occur on the date provided in such notice whether or not a Liquidity Facility is provided after such initial notice has been given.

(c) Remarketing. On the Business Day on which the first notice is mailed pursuant to Section 1.6(b) of this Appendix F, the Paying Agent and Registrar shall notify the Tender Agent and the Remarketing Agent by telephone, telegram, telecopy, telex or other similar communication of the aggregate principal amount of Bonds to be tendered for purchase on the mandatory tender date.

The Remarketing Agent shall offer for sale at par and use its best efforts to find purchasers for the portion of Bonds to be tendered pursuant to Section 1.6(a) of this Appendix F and advise them whether the Liquidity Facility will be replaced. In the case of replacement of the Liquidity Facility, the State shall give notice to the Paying Agent and Registrar, and the Paying Agent and Registrar shall provide written notice to the Remarketing Agent, which shall inform prospective purchasers of the identity of the new Liquidity Provider and the ratings to be in effect on the Bonds following such replacement. All Bonds shall be at all times remarketed at a price equal to the principal amount thereof, plus the interest thereon accrued up to the remarketing date.

Section 1.7 Purchase of Tendered Bonds.

(a) Notices; Draws on Liquidity Facility. At or before 3:30 p.m., New York City time, on the Business Day immediately preceding the Purchase Date (or 11:00 a.m., New York City time, on the Purchase Date in the case of Bonds the interest on which is determined at Daily Rates), the Remarketing Agent shall give notice by telephone, telegram, telecopy, telex or other similar communication to the State, the Paying Agent and Registrar and the Liquidity Provider of the principal amount of tendered Bonds which have not been remarketed and of the names, addresses and taxpayer identification numbers of the purchasers and the denominations of remarketed Bonds to be delivered to each purchaser. On the Purchase Date, the Paying Agent and Registrar shall draw on the Liquidity Facility to timely pay the Purchase Price with regard to the Bonds for which remarketing proceeds (other than proceeds of sale to the State) have not been paid to the Paying Agent and Registrar. In the event that the Paying Agent and Registrar does not receive from the Remarketing Agent the notice described in this Section 1.7(a), on the Purchase Date the Paying Agent and Registrar shall draw on the Liquidity Facility to the extent necessary to timely pay the Purchase Price of all Bonds subject to tender for purchase on such Purchase Date. In the case of a Purchase Date which is a Substitution Date, the Liquidity Facility, if any, on which the Paying Agent and Registrar draws shall be the Liquidity Facility for which a replacement is being provided on such Substitution Date. Notwithstanding the foregoing, the Paying Agent and Registrar shall not draw on the Liquidity Facility to pay the Purchase Price of Bonds tendered by the State or the Liquidity Provider.

(b) Sources of Payment. The Remarketing Agent shall pay to the Paying Agent and Registrar, by 10:30 A.M. on the Purchase Date, all amounts representing proceeds of the remarketing of tendered Bonds, such payments to be made in the manner specified in Section 1.7(c) of this Appendix F. All such proceeds, the proceeds of a draw upon the Liquidity Facility and all other available moneys shall be held by the Paying Agent and Registrar in trust for the benefit of the Owners of the Bonds. **The State shall not be obligated to provide funds for the payment of the Purchase Price of Bonds upon any tender.**

(c) Payments by the Paying Agent and Registrar. Before 4:00 p.m., New York City time, on the Purchase Date and upon receipt by the Paying Agent and Registrar of 100% of the aggregate Purchase Price of the tendered Bonds, the Paying Agent and Registrar shall pay the Purchase Price of such Bonds to the Owners thereof (or as otherwise provided in Section 1.4 of this Appendix F) at its principal office or, if requested, by bank

wire transfer. Such payments shall be made in immediately available funds. Payments of such Purchase Price are to be made from the following sources in the order of priority indicated:

(i) The proceeds of the sale of the Bonds which have been remarketed by the Remarketing Agent (other than proceeds of a sale of the Bonds to the State); and

(ii) The proceeds of the sale of the Bonds which have been purchased by the Liquidity Provider pursuant to the Liquidity Facility or other proceeds received under or pursuant to a Liquidity Facility; and

(iii) Moneys paid by the State for such purpose. **The State shall not be obligated to provide funds for the payment of the Purchase Price of Bonds upon any tender.**

(d) Registration and Delivery of Tendered or Purchased Bonds.

(i) Subject to the requirements of paragraphs (ii) and (iii) immediately below, on the Purchase Date, the Paying Agent and Registrar shall register and deliver (or hold) all Bonds purchased on any Purchase Date as follows:

(1) Bonds purchased or remarketed by the Remarketing Agent shall be registered in accordance with the instructions of the Remarketing Agent and made available for delivery to the Remarketing Agent; and

(2) Bonds purchased with funds made available under or pursuant to the Liquidity Facility shall be registered in the name of the Liquidity Provider or its nominee, designee or assignee and shall be held by the Paying Agent and Registrar in trust for the benefit of the Liquidity Provider or its nominee, designee or assignee or shall be delivered to or to the order of the Liquidity Provider, all in accordance with the provisions of the Liquidity Facility. While so registered, such Bonds shall constitute Provider Bonds.

(ii) While a Book-Entry-Only System is in effect for the Bonds, the Paying Agent and Registrar shall deliver Bonds purchased or remarketed by the Remarketing Agent by transfer of beneficial ownership of such Bonds on the registration books of DTC to or upon the order of the Remarketing Agent.

(iii) While a Book-Entry-Only System is in effect for the Bonds, the Paying Agent and Registrar shall cause Bonds purchased with funds made available under or pursuant to the Liquidity Facility to be registered in the name of the Liquidity Provider or its designee, nominee or assignee on the registration books of DTC. Notwithstanding the foregoing, to the extent required by the Liquidity Facility, the Paying Agent and Registrar shall withdraw Provider Bonds from the Securities Depository and shall prepare and authenticate physical Bonds representing such Provider Bonds. While a Book-Entry-Only System is in effect for the Bonds, in the event that Provider Bonds which are not held under the Book-Entry-Only System are subsequently remarketed, the Paying Agent and Registrar shall take such action as shall be necessary to reinstate the Book-Entry-Only System for such Bonds and shall transfer beneficial ownership thereof on the books of DTC to or upon the order of the Remarketing Agent.

(e) Delivery of Bonds; Effect of Failure to Surrender Bonds.

(i) All Bonds to be purchased on any date shall be required to be delivered to the designated corporate trust office of the Tender Agent at or before 11:30 a.m., New York City time, on the Purchase Date, except that while the interest thereon is determined at Semiannual or Extended Rates, Bonds being tendered for purchase at the election of the Owner pursuant to Section 1.4 of this Appendix F shall be delivered to the designated corporate trust office of the Tender Agent along with the notice of tender.

(ii) If the Owner of any Bond (or portion thereof) that is subject to purchase fails to surrender such Bond to the Tender Agent for purchase when required by paragraph (i) of this subsection (e) or by

Section 1.4 of this Appendix F, and if the Paying Agent and Registrar is in receipt of the Purchase Price therefor, such Bond (or portion thereof) shall nevertheless be deemed purchased on the Purchase Date and ownership of such Bond (or portion thereof) shall be transferred to the purchaser thereof as provided in subsection (d) of this Section 1.7. Any Owner who fails to deliver a Bond for purchase as required above shall have no further rights thereunder except the right to receive the Purchase Price thereof upon presentation and surrender of said Bond to the Tender Agent. The Tender Agent shall promptly notify the Paying Agent and Registrar of any such failure to deliver a Bond to the Tender Agent, and the Paying Agent and Registrar shall be entitled to conclusively rely on such notification.

(f) Investment of Funds. All money held by the Paying Agent and Registrar for the payment of the Purchase Price of Bonds from whatever source derived, including remarketing proceeds and draws upon the Liquidity Facility, shall be held in a separate segregated account and shall be held uninvested.

(g) Exception for Bonds Owned by State. Notwithstanding anything in this Series Certificate to the contrary, the Liquidity Provider shall not be required to purchase Bonds subject to optional or mandatory tender for purchase under this Series Certificate that are beneficially held (or held in certificated form) by or on behalf of the State.

Section 1.8 Bonds Purchased Under Liquidity Facility. In the event that any Bonds are Provider Bonds, such Bonds shall be held in accordance with Section 1.7(d) of this Appendix F and the Remarketing Agent shall continue to offer for sale and use its best efforts to sell such Bonds at a price equal to the principal amount thereof, plus the interest thereon accrued up to the remarketing date. While the Liquidity Facility is effective, Bonds purchased with funds made available under the Liquidity Facility shall not be delivered upon remarketing unless the Liquidity Facility is reinstated for the principal amount thereof and interest thereon in accordance with its terms and the Remarketing Agent, the Paying Agent and Registrar, the Tender Agent and any designee of the Liquidity Provider then holding Provider Bonds have been advised in writing by the Liquidity Provider that it has elected to reinstate the Liquidity Facility in full.

Section 1.9 Mandatory Tenders Upon Conversion to Fixed Rate.

(a) Purchase Date. In the case of any conversion of the interest on the Bonds from a Variable Rate Period to the Fixed Rate Period, the Bonds to be converted are subject to mandatory tender for purchase on the Conversion Date at the Purchase Price.

(b) Notice to Owners. Any notice of a conversion given to Bondholders pursuant to Section 1.2(o) of this Appendix F shall, in addition to the requirements of such Section, specify that the Bonds to be converted will be subject to mandatory tender for purchase on the Conversion Date and the time at which Bonds are to be tendered for purchase.

(c) Remarketing. At or before 4:00 p.m., New York City time, on the fifteenth calendar day (or, if such day is not a Business Day, on the next succeeding Business Day) preceding the conversion to a Fixed Rate Period, the Paying Agent and Registrar shall notify the Tender Agent, the Liquidity Provider and the Remarketing Agent, by telephone, telegram, telecopy, telex or other similar communication, of the aggregate principal amount of Bonds to be tendered for purchase on the Conversion Date. The Remarketing Agent shall offer for sale and use its best efforts to find purchasers for the aggregate principal amount of Bonds to be tendered.

Section 1.10 Insufficient Funds for Purchases. If the moneys available for purchase of Bonds are inadequate for the purchase of all Bonds which are tendered on any Purchase Date, the interest thereon subject to such purchase shall be determined at a rate which is the lesser of (i) a rate established by the Remarketing Agent or (ii) the Maximum Rate, to the date on which the earliest of the following occurs:

(a) The Fixed Rate Conversion Date, or the Conversion Date for any other Rate Period if a Liquidity Facility is in place pursuant to the Resolution;

(b) The date on which any default by the Liquidity Provider under the terms of the Liquidity Facility has been cured; or

(c) The effective date of a new interest rate established by the Remarketing Agent which is less than the Maximum Rate after the date on which an Alternate Liquidity Facility meeting the requirements of the Resolution becomes effective.

If the preceding provisions of this Section become applicable, (i) the Tender Agent shall immediately (but no later than the end of the next succeeding Business Day) return all tendered Bonds to the Owners thereof and notify all Owners of Bonds in writing of the rate at which the interest thereon will be determined pursuant to the preceding provisions of this Section and (ii) the Paying Agent and Registrar shall return all moneys received for the purchase of such Bonds to the Persons who provided such moneys; provided, however, that the Owners shall retain all rights to tender the Bonds pursuant to the provisions of this Series Certificate and the obligation of the State to honor such tenders shall remain in effect until payment therefor has been provided in accordance with the provisions of this Series Certificate. **Notwithstanding the foregoing, the State shall not be obligated to provide funds for the payment of the Purchase Price of Bonds upon any tender.**

Section 1.11 Book-Entry Tenders. Notwithstanding any other provision of this Appendix F to the contrary, all tenders for purchase during any period in which the Bonds are maintained in a Book-Entry-Only System, shall be subject to the terms and conditions set forth in any agreement among the State, the Paying Agent and Registrar and DTC and any rules and regulations promulgated by DTC.

Section 1.12 Duties of Paying Agent and Registrar with Respect to Purchase of Bonds. The Paying Agent and Registrar agrees, with respect to any optional or mandatory tender of the Bonds:

(a) to hold all moneys, other than moneys delivered to it by or on behalf of the State for the purchase of Bonds, delivered to it hereunder for the purchase of Bonds as agent and bailee of and in escrow for the benefit of, the Person or entity which shall have so delivered such moneys until the Bonds purchased with such moneys shall have been delivered to or for the account of such Person or entity; and

(b) to hold all moneys delivered to it hereunder by or on behalf of the State for the purchase of Bonds as agent and bailee of, and in escrow for the benefit of, the Owners who shall deliver Bonds to it for purchase until the Bonds purchased with such moneys shall have been delivered to or for the account of the State.

Section 1.13 No Tender of Provider Bonds. Provider Bonds shall not be subject to tender for purchase.

Section 1.14 No Mandatory Tender Upon Special Termination Event. Notwithstanding anything to the contrary contained in this Appendix F, upon the occurrence of a Special Termination Event, there will be no mandatory tender of the Bonds and the obligation of the Liquidity Provider to purchase the Bonds pursuant to the Liquidity Facility will cease without prior notice to holders of the Bonds. The State shall not be obligated to provide funds for the payment of the Purchase Price of Bonds upon any tender.

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